

No. 15334

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United States  
Court of Appeals  
for the Ninth Circuit

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LUCKY LAGER BREWING COMPANY,  
Petitioner,  
vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States

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## INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

### PAGE

Acknowledgement of Service of Designation of Record on Review.....	56
Answer .....	24
Appearances .....	1
Clerk's Certificate .....	96
Decision .....	49
Designation of Record on Review .....	55
Docket Entries .....	3
Finding of Facts and Opinion .....	34
Notice of Filing Petition for Review .....	54
Proof of Service .....	55
Petition .....	5
Petition for Review .....	50
Proceedings .....	56
Witnesses, Petitioner's:	
Baird, Walter M.	
—direct .....	76
—cross .....	87

## Witnesses, Petitioner's—(Continued):

Jordan, Fred W.

—direct .....	57
—cross .....	66
—redirect .....	73
—recross .....	74

Statement of Points and Designation of Record (U.S.C.A.) .....	98
Stipulation of Facts .....	25
Exhibit 1 (Designated Portions) .....	31
Stipulation Re Exhibits (U.S.C.A.) .....	100

## APPEARANCES

For Petitioner:

ARTHUR H. KENT, ESQ.;  
VALENTINE BROOKES, ESQ.;  
PAUL E. ANDERSON, ESQ.;  
RUSSEL SHEARER, ESQ.

For Respondent:

AARON S. RESNICK, ESQ.





The Tax Court of the United States

Docket No. 53063

LUCKY LAGER BREWING COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1954

May 24—Petition received and filed. Taxpayer notified. Fee paid.

May 25—Copy of petition served on General Counsel.

May 24—Request for Circuit hearing in San Francisco, Calif., filed by taxpayer. 5/28/54. Granted.

July 8—Answer filed by General Counsel.

July 13—Copy of answer served on taxpayer, San Francisco, Calif.

1955

June 24—Hearing set Oct. 3, 1955, San Francisco, Calif.

Oct. 11—Hearing had before Judge Oppen on the merits. Entry of appearance of Valentine Brookes, Esq., and Russel Shearer, Esq., and Stipulation of Facts with Exhibits I, II, III, IV and V attached, filed at hearing. Petitioner's Brief due 11/25/55; Respondent's Brief due 1/9/56; Petitioner's Reply Brief due 2/8/56.

- Oct. 31—Transcript of Hearing 10/4/55 filed.
- Nov. 10—Stipulation to correct transcript, embodying corrections, filed.
- Nov. 17—Motion for extension to Dec. 16, 1955, to file brief filed by taxpayer. 11/18/55. Granted.
- Dec. 15—Brief filed by taxpayer. 12/16/55. Copy served.

## 1956

- Jan. 30—Answer Brief filed by Respondent. Served 1/31/56.
- Feb. 23—Motion for extension to Mar. 25, 1956, to file reply brief filed by taxpayer. 2/24/56. Granted.
- Mar. 27—Reply Brief filed by Petitioner. 3/27/56. Served.
- July 19—Findings of Fact and Opinion filed, Judge Oppen. Decision will be entered for the Respondent. Served 7/19/56.
- July 23—Decision entered, Judge Oppen, Div. 14, Served 7/25/56.
- Sept. 27—Petition for Review by U. S. Court of Appeals for the Ninth Circuit filed by Petitioner.
- Sept. 28—Notice of filing petition for review, with proof of service thereon, filed by petitioner.
- Oct. 3—Designation of record on review, with proof of service thereon, filed by petitioner.
- Oct. 3—Acknowledgment of service of designation of the record on review, filed by respondent.

[Title of Tax Court and Cause.]

## PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (symbols Ap:SF:AA:EWM 90-D:WHLY) dated April 6, 1954, and as a basis of its proceeding alleges as follows:

1. Petitioner is a corporation organized and existing under the laws of the State of California, with its principal office at 2601 Newhall Street, San Francisco 19, California. Petitioner's business is the brewing and sale of beer for consumption. Its return for the period here involved was filed with the Collector for the Northern District of California at San Francisco. Petitioner keeps its books and makes its income tax returns upon the accrual basis. Petitioner's taxable year is and has been for all years relevant to this proceeding the calendar year.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to petitioner by registered mail on April 6, 1954.

3. The taxes in controversy are income and excess profits taxes for the taxable year ended December 31, 1950, in the amount of \$92,108.20.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) Respondent erred in determining that petitioner satisfies neither of the tests of growth required by Section 435(e)(1)(A)(ii) of the Internal Revenue Code and in consequence is not a growth corporation entitled to the benefits of Section 435(e) of said Code.

(b) Respondent erred in disallowing the excess profits credit of \$3,294,575.86 claimed in petitioner's return and in his further determination that petitioner was not entitled to an excess profits credit for said year in an amount in excess of \$2,703,934.03.

5. The facts upon which petitioner relies as the basis of this proceeding are as follows:

(a) In the computation of petitioner's gross receipts for the taxable years constituting its base period, to wit: the calendar years 1946, 1947, 1948 and 1949, in connection with the application of the growth test prescribed by Section 435(e)(1)(A)(ii), Internal Revenue Code (see Exhibit B on page 10 of the Statement attached to and forming a part of the notice of deficiency), respondent erroneously omitted and excluded the amounts set forth and described in the following subparagraphs:

(1) Petitioner derived from the sale of spent grains and sacks during its taxable years 1946, 1947, 1948 and 1949 the sums of \$24,030.47, \$28,292.45, \$29,201.88, and \$35,187.79. Such amounts constituted gross income attributable to the trade or business of petitioner.

(2) Petitioner derived from the sale of yeast during its taxable years 1946, 1947, 1948 and 1949, respectively, the sums of \$3,476.61, \$4,755.06, \$7,670.25, and \$11,747.47. Such amounts constituted income attributable to the trade or business of petitioner.

(b) In the computation of petitioner's gross receipts for the aforesaid taxable years constituting its base period, in connection with the application of the growth test prescribed by Section 435(e) (1)(A)(ii), Internal Revenue Code (see Exhibit B on page 10 of the Statement attached to and forming a part of the notice of deficiency), respondent erroneously included the amounts set forth and described in the following subparagraphs:

(1) The amounts shown under the heading of Miscellaneous on line 6 of said Exhibit B, viz., \$1,071.96, \$41.13 (\$126.98), and \$25.45 for petitioner's taxable years 1946, 1947, 1948 and 1949 aforesaid, represent sums derived from the sale of scrap, checks written off, and unclaimed container deposits. Amounts derived from the sale of scrap are expressly excluded under Section 435(e)(5)(B) (i), Internal Revenue Code, as proceeds from the sale of property, while amounts derived from checks written off and unclaimed container deposits are expressly excluded under Section 435(e)(5)(B)(ii) as income derived from the discharge of indebtedness.

(2) Petitioner derived interest on United States bonds in the amounts of \$18,886.51 for its taxable



year 1946 and \$19,102.75 for its taxable year 1947, while for its taxable year 1948 petitioner sustained a loss in the amount of \$4,518.26 by cashing in before their maturity discount United States bonds on which interest had been accrued theretofore. (See Exhibit B aforesaid, line 3). Such bond interest and loss were not income or loss attributable to petitioner's trade or business.

(3) The item labeled "Judgment" on line 7 of Exhibit B aforesaid, to wit: \$3,139.88 for petitioner's taxable year 1947, represents the settlement in that year of a suit instituted by petitioner many years before against a supplier of barrels on account of bad barrels shipped to petitioner in the year 1933.

(4) The amounts shown on line 5 of Exhibit B aforesaid under the caption "Discount received," to wit: \$11,642.97, \$26,314.59, \$27,108.96, and \$43,530.23 for petitioner's taxable years 1946, 1947, 1948 and 1949, respectively, represent trade discounts received by petitioner during said years on various materials and supplies purchased by it. They constituted as such reductions in the cost of such materials and supplies and not gross receipts of petitioner's trade or business.

(5) The figure of \$13,692.82 for petitioner's taxable year 1947 and the figure of \$1,713.33 for petitioner's taxable year 1948, shown on lines 8 and 9 of Exhibit B aforesaid, represent, as their caption indicates, quantity discounts on cans purchased received by petitioner during said years. They constituted as such reductions in the cost of cans

purchased and not gross receipts of petitioner's trade or business.

(6) The figures shown in line 1 of Exhibit B aforesaid under the caption "Gross Sales," to wit: \$12,878,751.99, \$16,311,138.47, \$18,161,135.39, and \$23,003,696.22 for petitioner's taxable years 1946, 1947, 1948 and 1949, respectively, include the amounts for such years of the federal stamp tax imposed by Section 3150 of the Internal Revenue Code "\* \* \* on all beer \* \* \* brewed or manufactured and sold, or removed for consumption or sale, within the United States, or imported into the United States, \* \* \*," and the excise tax "\* \* \* upon all beer \* \* \* sold in this state by a manufacturer \* \* \*," imposed by Section 23 of the Alcoholic Beverage Control Act, being Act 3796 of the General Laws of the State of California, and paid by petitioner. The amounts included in gross sales which represent the total of these two taxes are \$4,849,076.70 for petitioner's taxable year 1946, \$5,687,831.75 for the taxable year 1947, \$5,908,185.09 for the taxable year 1948, and \$7,192,289.27 for the taxable year 1949. The aforesaid taxes constitute excise taxes levied upon petitioner for the sale or removal of beer for consumption and their amount is not properly includible in the computation of petitioner's gross receipts for the purposes of Section 435(e)(1)(A)(ii) of the Internal Revenue Code.

Wherefore, petitioner prays that this Honorable Court may hear the proceeding and that the Court

shall determine that there is no deficiency in the income tax and excess profits tax liability of petitioner for its taxable year ended December 31, 1950, in excess of \$10,235.74.

/s/ ARTHUR H. KENT,

/s/ VALENTINE BROOKES,

/s/ PAUL E. ANDERSON,

/s/ RUSSEL SHEARER,

Counsel for Petitioner.

State of California,

City and County of San Francisco—ss.

Eugene S. Selvage, being duly sworn, says that he is the President of Lucky Lager Brewing Company, the corporation named as petitioner in the above proceeding, and as such is duly authorized to verify the foregoing petition; that he has read said petition and is familiar with the statements contained therein, and that the facts stated therein are true to the best of his knowledge, information and belief.

[Seal] /s/ EUGENE S. SELVAGE.

Subscribed and sworn to before me this 18th day of May, 1954.

[Seal] /s/ MARGARET ENNIS,

Notary Public in and for the City and County of San Francisco, State of California.

My commission expires June 6, 1955.



U. S. Treasury Department  
Office of the Regional Commissioner  
Internal Revenue Service  
Appellate Division—San Francisco Region  
Room 710 - 630 Sansome Street  
San Francisco 11, California

In Replying Refer to:

Ap:SF:AA:EWM

90-D:WHLy

April 6, 1954.

Lucky Lager Brewing Company  
2601 Newhall Street  
San Francisco 19, California

Gentlemen:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1950, discloses a deficiency of \$102,-343.94 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday or legal holiday in the District of Columbia, in which event that day is not counted as the 90th

day. Otherwise Saturdays, Sundays and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Assistant Regional Commissioner, Appellate, Room 710, 630 Sansome Street, San Francisco 11, California. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earlier.

Very truly yours,

T. COLEMAN ANDREWS,  
Commissioner;

By /s/ WM. H. LAWDER,  
Associate Chief, Appellate  
Division.

Enclosures:

Statement

Form 1276

Agreement

Exhibits A, B, & C

Ap:SF:AA:EWM

90-D:WHL:v

Statement

Lucky Lager Brewing Company

2601 Newhall Street

San Francisco 19, California

Tax liability for the taxable year ended December 31, 1950

	Deficiency
Income Tax .....	\$102,343.94

In making this determination of your income tax liability, careful consideration has been given to your protest dated August 20, 1953, and to the statements made at the conference held on November 25, 1953.

A copy of this letter and statement has been mailed to your representative, Mr. Russel Shearer, c/o Shearer & Thomas, 1 Montgomery Street, San Francisco 4, California, in accordance with the authority contained in the power of attorney executed by you.

Year 1950

Adjustments to Net Income

Net income as disclosed by the original return .....		\$4,198,745.53
Unallowable deductions and additional income:		
(a) Adjustment of allowable deduction for Brewers' Association Dues .....		16,541.70
(b) Adjustment of deduction for cash discounts .....		11,455.70
		<hr/>
Total .....		\$4,226,742.93
Nontaxable income and additional deductions:		
(c) Adjustment of deduction for vacation pay .....	\$1,034.42	
(d) Adjustment of deduction for depreciation .....	1,768.76	
(e) Adjustment of deduction for franchise tax .....	823.42	3,626.60
		<hr/>
Net income as adjusted.....		\$4,223,116.33

## Explanation of Adjustments

(a) Net income is increased \$16,541.70, representing an adjustment of the allowable deduction for Brewers' Association Dues. Computation of adjustment is shown below:

Amount paid to California State Brewers'

Institute as contributions to the Public  
Relations Fund at the rate of 5c per

barrel .....\$ 51,632.74

Percentage of above payment held to be

unallowable ..... 82.0372295%

Amount of payment unallowable as revised

(82.0372295% of \$51,632.74) .....\$ 42,358.07

Amount of payment unallowable as shown

by the original return ..... 25,816.37

Increase in net income (additional amount

unallowable) .....\$ 16,541.70

(b) Net income is increased \$11,455.70, representing an adjustment of deduction for Cash Discounts.

Deduction for Cash Discounts taken on the

original return .....\$ 11,455.70

Allowable deduction for Cash Discounts..... None

Increase in net income.....\$ 11,455.70

(c) Net income is decreased \$1,034.42, representing an adjustment of the accrual in the year 1950 for vacation payments to be made in the year 1951.

Deduction claimed in the original return for

accrual of vacation payments .....\$117,052.55

Vacation payments made in the year 1951.... 118,086.97

Decrease in net income.....\$ 1,034.42

(d) Net income is decreased \$1,768.76, representing the allowance of an additional deduction for depreciation. See Exhibit A.

(e) Net income is decreased \$823.42, representing an adjustment of deduction for franchise tax.

Computation of adjustment is shown below:

Additional income for the year 1949 as per Revenue Agent's report for that year.....	\$ 20,782.58
Less: Franchise tax adjustment for the year 1949 by Revenue Agent's report.....	197.01
<hr/>	
Additional 1949 income for franchise tax purposes .....	\$ 20,585.57
<hr/>	
Additional allowable deduction for franchise tax (4% of \$20,585.57) .....	\$ 823.42

Computation of Income Tax

Net income .....	\$4,223,116.33
Less: Dividends received credit.....	None
<hr/>	
Normal-tax net income .....	\$4,223,116.33
<hr/>	
Normal tax on \$4,223,116.33 at 23%.....	\$ 971,316.76
<hr/>	
Net income .....	\$4,223,116.33
Less: Dividends received credit.....	None
<hr/>	
Surtax net income .....	\$4,223,116.33
<hr/>	
Surtax on \$25,000.00 .....	None
<hr/>	
Surtax on \$4,198,116.33 at 19%.....	\$ 797,642.10
<hr/>	
Total normal tax and surtax.....	\$1,768,958.86
Add: Excess profits tax.....	230,686.42
<hr/>	
Income tax liability .....	\$1,999,645.28
<hr/>	
Income tax assessed:	
Original Account No. 419107, September, 1951	
List. First California District .....	1,897,301.34
<hr/>	
Deficiency in income tax .....	\$ 102,343.94

## Adjustments to Excess Profits Net Income

Excess profits net income as disclosed by the original return .....	\$4,210,899.27
Unallowable deductions and additional income:	
(a) Net increase in income tax net income.....	24,370.80
Total .....	<u>\$4,235,270.07</u>
Nontaxable income and additional deductions:	
(b) Elimination of net loss from sale of property .....	5,963.86
Excess profits net income as adjusted.....	<u>\$4,229,306.21</u>

## Explanation of Adjustments

(a) Excess profits net income is increased \$24,370.80, representing net increase in income tax net income.

(b) Excess profits net income is decreased \$5,963.86, representing the elimination of a loss on sale of property other than capital assets which was erroneously added to excess profits net income in the original return.

## Computation of Excess Profits Tax

Excess profits net income .....	\$4,229,306.21
Less: Excess profits credit .....	2,703,934.03
Adjusted excess-profits net income..	<u>\$1,525,372.18</u>
30% of adjusted excess-profits net income .....	<u>\$ 457,611.65</u>
62% of excess profits net income....	\$2,622,169.85
Less: Normal tax and surtax on excess-profits net income:	
42% of \$4,229,306.21.....	\$1,776,308.61
Less: .....	<u>4,750.00</u> 1,771,558.61
Balance .....	<u>\$ 850,611.24</u>
Above balance, or 30% of adjusted excess-profits net income, whichever is the lesser amount.....	<u>\$ 457,611.65</u>
Excess profits tax (184/365ths of \$457,611.65) .....	<u>\$ 230,686.42</u>



Base Period Net Income	As Disclosed by Return	Additions (Deductions)	Corrected
Excess profits net income:			
Year ended Dec. 31, 1946.....	\$2,049,770.13 (a)	(\$36,235.32)	\$2,013,534.81
Year ended Dec. 31, 1947.....	2,081,585.90 (b)	( 3,625.38)	2,077,960.52
Year ended Dec. 31, 1948.....	2,341,402.92 (c)	3,643.40	2,345,046.32
Year ended Dec. 31, 1949.....	3,846,016.32 (d)	16,068.49	3,862,084.81
Aggregate of 3 highest years.....	\$8,269,005.14	\$16,086.51	\$8,285,091.65
Average base period net income.....	\$2,756,335.04	\$ 5,362.18	\$2,761,697.22
Base period net income—			
Alternative based on growth.....	\$3,846,016.32		Not applicable see adjustment (e)
Average base period net income.....	\$3,846,016.32		\$2,761,697.22
Excess Profits Credit			
85% of average base period net income of			
\$2,761,697.22 .....			\$2,347,442.64
Add: 12% of base period capital addition, See Exhibit C .....			331,029.40
12% of net capital addition as shown by the return .....			25,461.99
Excess profits credit .....			\$2,703,934.03

Explanation of Adjustments to  
Excess Profits Credit

(a) Abnormal deduction of \$36,235.32 is restored, since the deduction does not exceed 5% of the 4 year average base period excess profits net income. Section 433(b)(10)(B) Internal Revenue Code.

(b) Abnormal deduction of \$3,625.38 is restored, since the deduction does not exceed 5% of the 4 year average base period excess profits net income. Section 433(b)(10)(B) Internal Revenue Code.

(c) Excess profits net income for the year 1948 is increased \$3,643.40. Computation of adjustment is shown below:

Normal tax net income for the year 1948 as shown	
by the Revenue Agent's report.....	\$2,349,415.33
Normal tax net income for the base period year	
1948 as shown by the 1950 return.....	2,345,771.93

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Increase in excess profits net income.....	\$ 3,643.40
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(d) Excess profits net income for the year 1949 is increased \$16,068.49. Computation of adjustment is shown below:

Normal tax net income for the year 1949 as shown	
by the Revenue Agent's report.....	\$3,859,549.58
Normal tax net income for the base period year	
1949 as shown by the 1950 return.....	3,838,767.00

---

Increase in excess profits net income.....	\$ 20,782.58
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Less:

Restoration of abnormal deduction of \$4,714.09 claimed in the original return, since the deduc- tion does not exceed 5% of the 4 year average base period excess profits net income in accord- ance with Section 433 (b) (10) (B) Internal Revenue Code .....	4,714.09
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Net increase in excess profits net income.....	\$ 16,068.49
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(e) The excess profits credit of \$3,294,575.86 claimed in your return as a growth corporation entitled to the benefits of Section 435(e) of the Internal Revenue Code has been adjusted to eliminate the benefits of that section. It is held that neither of the tests of growth required by Section 435(e)(1)(A)(ii) has been met. See Exhibit B.



# EXHIBIT A

## Adjustment in Allowable Depreciation

Item	Date Acquired	Cost	Rate of Depreciation	Allowable Depreciation	Corrected Reserve 12-31-49	Corrected Reserve 12-31-50
Canopies on Warehouse #3.....	4/11/46	\$ 1,685.00	21½%	\$ 42.13	\$ 157.98	\$ 200.11
Roof sign .....	10/31/47	3,605.00	6⅔%	240.45	520.97	761.42
Paving main truck driveway.....	11/29/47	8,851.15	10 %	885.12	1,844.00	2,729.12
Wiring #6 bottle line.....	5/31/48	2,955.05	12½%	369.38	584.85	954.23
4 sets attachments to rotary labelers .....	10/12/48	1,853.46	12½%	231.68	289.60	521.28
Totals .....		\$18,949.66		\$1,768.76	\$3,397.40	\$5,166.16
Depreciation claimed on the origi- nal return .....				None		
Additional depreciation allowable				\$1,768.76		

## EXHIBIT B

## Growth Test Under Section 435(e)(1)(A)(ii)

## Internal Revenue Code

## (Gross Receipts During the Base Period)

	1946	1947	1948	1949
Gross Sales .....	\$12,878,751.99	\$16,311,138.47	\$18,161,135.39	\$23,003,696.22
Interest .....	766.88	749.99	4,284.73	1,360.56
Interest on U. S. Bonds .....	18,886.51	19,102.75	(4,518.26)	—
Royalties .....	45,000.00	45,000.00	45,000.00	45,000.00
Other Income:				
Discount received .....	11,642.97	26,314.59	27,108.96	43,530.23
Miscellaneous .....	1,071.96	41.13	(126.98)	25.45
Judgment .....	—	3,139.88	—	—
Quantity discount rebate on cans purchased:				
Year 1947 .....		13,692.82		
Year 1948 .....			1,713.33	
Gross receipts, Section 435(e)(5) .....	\$12,956,120.31	\$16,419,179.63	\$18,234,597.17	\$23,093,612.46
Total, last half of base period .....			\$41,328,209.63	
Total, first half of base period .....			\$29,375,299.94	
Ratio of last half to first half .....			140.69%	

EXHIBIT C  
Base Period Capital Addition

	(Col. 1) Year 1950	(Col. 2) Year 1949	(Col. 3) Year 1948
Equity capital beginning of year .....	\$7,656,119.07	\$5,664,828.80	\$4,621,658.89
75% of borrowed capital beginning of year.....	318,750.00	—	—
Total .....	\$7,974,869.07	\$5,664,828.80	\$4,621,658.89
Adjustment for interest on borrowed capital .....	\$ 97,395.83	—	—
Total .....	\$7,974,869.07	\$5,664,828.80	\$4,621,658.89
75% thereof .....	\$ 73,046.87	—	—
Yearly base period capital	\$7,901,822.20	\$5,664,828.80	\$4,621,658.89
Excess of Column 1 over the higher of Column 2 or Column 3 .....			\$2,236,993.40
50% of excess of Column 2 over Column 3.....			521,584.96
Base period capital addition			\$2,758,578.36
12% of base period capital addition .....			\$ 331,029.40
Total assets as shown by the return .....	\$10,463,951.42	\$7,209,490.83	\$6,155,228.98
Total liabilities as shown by the return .....	2,838,580.98	1,575,194.55	1,573,608.22
Equity capital as shown by the return .....	\$7,625,370.44	\$5,634,296.28	\$4,581,620.76
Additional income as shown by Revenue Agent's re- ports: 1946-1947-1948 .....	42,378.18	42,378.18	56,464.31
1949 .....	12,533.59	—	—
1945 tax refund .....		4,420.10	4,420.10
Total .....	\$7,680,282.21	\$5,681,094.56	\$4,642,505.17

	(Col. 1) Year 1950	(Col. 2) Year 1949	(Col. 3) Year 1948
Deduct additional income tax: 1946-1947-1948 .....	14,881.27	14,881.27	20,846.9
1948-1949 .....	9,281.87	1,384.49	—
Equity capital as corrected	\$7,656,119.07	\$5,664,828.80	\$4,621,658.3
(b) Notes payable January 1, 1950, as shown by Schedule L of the original return....			\$ 425,000.0
75% thereof .....			\$ 318,750.0
(c) Notes outstanding Decem- ber 31, 1949, per book account 87 .....			\$ 425,000.0
Interest rate (American Trust Co.) .....			2 $\frac{3}{4}$
Annual interest .....			\$ 11,687.5
Annual interest multiplied by 100 .....			\$1,168,750.0
Adjustment for interest on borrowed capital (\$1,168,- 750.00 divided by 12) .....			\$ 97,395.8
(d) 75% of adjustment for in- terest on borrowed capital in accordance with the pro- visions of Section 435(f) (1) (C) of the Internal Revenue Code (75% of \$97,395.83) .....			\$ 73,046.8

Form 870 (1951)  
U. S. Treasury Department  
Internal Revenue Service

Lucky Lager Brewing Company  
2601 Newhall Street  
San Francisco 19, California

Ap:SF:AA:EWM  
90—D:WHLy

Waiver of Restrictions on Assessment and  
Collection of Deficiency in Tax  
and  
Acceptance of Overassessment

Pursuant to section 272 (d) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws, the restrictions provided in section 272 (a) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws are hereby waived and consent is given to the assessment and collection of the following deficiencies together with interest on the tax as provided by law; and the following over-assessments are accepted as correct:

Deficiencies

Type of Tax	Year Ended	Tax	Total
Income Tax.....	December 31, 1950	\$102,343.94	\$102,343.94

Form 870 (1951)

U. S. Treasury Department

Internal Revenue Service

Lucky Lager Brewing Company  
2601 Newhall Street  
San Francisco 19, California

Ap:SF:AA:EWM

90—D:WHLy

Waiver of Restrictions on Assessment and  
Collection of Deficiency in Tax  
and  
Acceptance of Overassessment

Pursuant to section 272 (d) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws, the restrictions provided in section 272 (a) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws are hereby waived and consent is given to the assessment and collection of the following deficiencies together with interest on the tax as provided by law; and the following over-assessments are accepted as correct:

Deficiencies

Type of Tax	Year Ended	Tax	Total
Income Tax.....	December 31, 1950	\$102,343.94	\$102,343.94

[Endorsed]: Filed May 24, 1954.

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[Title of Tax Court and Cause.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Daniel A. Taylor, Chief Counsel, Internal Revenue Service, and for answer to the petition filed by the

above-named petitioner, admits and denies as follows:

1, 2, and 3. Admits the allegations contained in paragraphs 1 to 3, inclusive, of the petition.

4(a) and (b). Denies the allegations of error contained in subparagraphs (a) and (b) of paragraph 4 of the petition.

5(a)(1) and (2), and (b)(1) to (6), inclusive. Denies the allegations contained in subparagraphs (a)(1) and (2) and (b)(1) to (6), inclusive, of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ DANIEL A. TAYLOR,      W.P.  
Chief Counsel, Internal  
Revenue Service.

[Endorsed]: Filed July 8, 1954.

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[Title of Tax Court and Cause.]

### STIPULATION OF FACTS

The following facts are stipulated to be true and may be accepted by the Court to the same extent as if established by competent evidence:



1. Petitioner is and has been for all years relevant to this proceeding a corporation organized and existing under the laws of the State of California, with its principal office at 2601 Newhall Street, San Francisco 19, California, petitioner's business being the brewing and sale of beer for consumption. Petitioner's returns for all years involved in the proceeding were filed with the Collector of Internal Revenue for the Northern District of California at San Francisco. Petitioner keeps its books and makes its income tax returns upon the accrual basis. Petitioner's taxable year is and has been for all years relevant to this proceeding the calendar year. For taxable years prior to the calendar year 1949, petitioner's corporate name was "General Brewing Corporation." On January 1, 1949, its corporate name was changed to "Lucky Lager Brewing Company."

2. Appended to this stipulation as Exhibit I are photostatic copies of United States Corporation Income Tax Returns (Form 1120) filed by petitioner for its taxable years 1946, 1947, 1948, 1949 and 1950. Such photostatic copies do not include certain schedules filed with the returns whose contents are irrelevant to any issue involved in the present proceeding.

3. Appended to this stipulation as Exhibit II is a schedule which accurately reflects figures appearing on petitioner's books of account and federal income tax returns for its taxable years 1946 to 1949, inclusive. The parties are agreed upon the



accuracy of these figures as figures, but the form in which the schedule is cast and the captions and terms used therein are intended by the parties to be and shall be without prejudice to the position of either party as to what constitutes "gross receipts" for the purposes of the growth test prescribed by Section 435(e)(1)(A)(ii), 1939 Internal Revenue Code. The figures at the top of the schedule at the head of the four columns opposite the term "Gross Sales" are the figures appearing in line 1 of petitioner's United States Corporation Income Tax Returns (Exhibit I hereto) for the four taxable years aforesaid, respectively. The amount of beer excise taxes paid in each of said years is included in the amount shown on line 2 of said returns opposite the term "Less: Cost of goods sold (from Schedule A)."

If the items shown as additions on the eight lines of the schedule below Gross Sales at the top of the schedule are held to constitute "gross income, attributable to a trade or business regularly carried on by the taxpayer \* \* \*" under Section 435(e)(5), 1939 Internal Revenue Code, then the figures representing "Ratio of last half to first half" contained in the schedule are correctly computed. The parties are agreed and so stipulate that the figures in the first line representing "Interest" and the figures in the sixth, seventh and eighth lines representing "Royalties," "Sales of Spent Grain & Sacks," and "Sales of Yeast" are proper additions in computing gross receipts under Section 435(e)(1)(A)(ii), but

petitioner reserves the right to question the includibility of the item "Interest on U. S. Bonds" on line 2, the item "Miscellaneous" on line 3, the item "Discount received" on line 4, and the item "Judgment" on line 5. It is stipulated that the effect of the elimination of these last four items from the computation will be to increase slightly the two ratios shown in the schedule as 140.67 and 150.30.

4. Appended to this stipulation as Exhibit III are true copies of five sales invoices sent by petitioner to customers. Said invoices are typical of the form of invoice used by petitioner during its base period years 1946 to 1949, inclusive.

5. Appended to this stipulation as Exhibit IV is a set of Lucky Lager Price Schedules promulgated at various times during petitioner's base period years 1946 to 1949, inclusive. The schedules included in this Exhibit are fairly typical of price schedules used during such years. Copies of all California schedules were regularly filed with the California Board of Equalization pursuant to law.

6. During petitioner's base period years 1946 to 1949, inclusive, petitioner's published annual reports reported under the caption "Gross Sales" the same amounts as on line 1 of its United States Corporation Income Tax Returns. The amounts paid by petitioner as federal and state excise taxes upon beer sold were not separately shown.

7. At all times herein material, the California Tax was paid by return on a month's sales on the 15th of the following month.

Up to March 1, 1950, and during all of the base period of taxpayer, under federal beer regulations the tax was paid by stamps purchased. The amount of stamps on hand was carried by taxpayer in an account entitled "Revenue Stamps on Hand," together with any state stamps held.

Under the federal beer regulations the tax was required to be paid prior to the time the beer was sold or delivered for consumption, and at the time the tanks were released by the Alcohol Tax Unit gauger to enable taxpayer to bottle its beer or fill cans with its beer.

The stamps surrendered from time to time when taxpayer bottled or canned its beer were transferred from the account "Revenue Stamps on Hand" to an account entitled "Tax on Bottled Beer," or "Tax on Canned Beer," as the case might be.

Unexpended beer stamps were not carried in the annual report under or as a part of the classification "Inventory," but were carried as a separate item under the heading "Current Assets."

If during the process of bottling, or later, beer was spoiled, was lost, or was sold to another brewer in bond, the amount of the stamps was refundable to taxpayer, and taxpayer credited the amount of such refunds to the proper accounts, to wit: "Tax on Bottled Beer" or "Tax on Canned Beer," as the case might be. In the case of one refund, where the refund was not obtained until substantially

later, such refund was included in taxpayer's books as "Miscellaneous Income" in 1949.

Effective March 1, 1950, the Treasury regulations relating to the collection of beer taxes were modified in the manner set forth in T.D. 5769, Federal Register, Jan. 31, 1950, 1950-1 CB, pp. 244, et seq.

The language of Section 3150 of the 1939 Internal Revenue Code, which imposed and described the federal excise tax on beer, was not in any way changed during any year herein material following 1945.

The attached Exhibit V consists of a photostatic copy of sheets from taxpayer's ledger accounts for the year 1948 and such accounts are some of the accounts to which reference has been made herein. These ledger accounts for the years 1946, 1947 and 1949 were maintained in the same manner.

8. If the Court shall find and adjudge that petitioner is entitled to the application of Section 435(e), 1939 Internal Revenue Code, in the determination of its excess profits tax credit based upon average base period net income, then the excess profits net income of petitioner for its taxable year 1949 as shown in the statutory notice of deficiency shall be reduced by the amount of \$70,772.21 and the excess profits net income of petitioner for its taxable year 1948 as shown in said statutory notice shall be increased by an identical amount.

9. Counsel for the respective parties reserve the right to object to the materiality or relevancy of

any matter contained in this stipulation, and also reserve the right to offer in evidence additional facts not in conflict with the facts herein stipulated as true.

/s/ ARTHUR H. KENT,

/s/ VALENTINE BROOKES,

/s/ PAUL E. ANDERSON,

/s/ RUSSEL SHEARER,  
Counsel for Petitioner.

/s/ JOHN POTTS BARNES,  
Chief Counsel, Internal Revenue Service, Counsel  
for Respondent.

## EXHIBIT No. 1

United States  
Corporation Income Tax Return  
For Calendar Year 1949

Corporation's Name and Address:

Lucky Lager Brewing Company  
2601 Newhall Street  
San Francisco 19, California

Date incorporated: 9/6/33.

State or County: California.

Principal business activity: Manufacturing.

Business group code number: 192.

Number of places of business: 3.

### Net Income Computation

#### Gross Income

Item and Instruction No.

1. Gross sales (where inventories are an income-determining factor); Less: Returns and allowances .....\$23,003,696.22



2. Less: Cost of goods sold. (From Schedule A) .....	17,132,484.68	
		<hr/>
3. Gross profit from sales.....	\$ 5,871,211.54	
4. Gross receipts (where inven- tories are not an income- determining factor) .....		
5. Less: Cost of operations. (From Schedule B) .....		
6. Gross profit where inventories are not an income-determining factor .....		
7. Interest on loans, notes, mort- gages, bonds, bank deposits, etc. ....	1,360.56	
		* * *
11. Royalties .....	45,000.00	
12. * * *		
(c) Net gain (or loss) from sale or exchange of property other than capital assets. (From Schedule D).....	(2,535.23)	
13. Dividends. (From Schedule E)		
14. Other income. (State nature)	119,669.07	
		<hr/>
15. Total income in items 3, and 6 to 14, inclusive.....		\$6,034,705.94

\* \* \*

United States  
Corporation Income Tax Return  
For Calendar Year 1950

Corporation's Name and Address:

Lucky Lager Brewing Company  
2601 Newhall Street  
San Francisco 19, California

Date incorporated: 9/6/33.

State or county: California.

Principal business activity: Malt Liquors.

Business group code number: 192.

Number of places of business: 4.

Net Income Computation

Gross Income

Item and Instruction No.

1. Gross sales (where inventories are an income-determining factor); Less: Returns and allowances .....\$30,467,131.41
2. Less: Cost of goods sold.  
(From Schedule A) ..... 22,736,644.70
3. Gross profit from sales.....\$ 7,730,486.71
4. Gross receipts (where inventories are not an income-determining factor) .....
5. Less: Cost of operations.  
(From Schedule B) .....
6. Gross profit where inventories are not an income-determining factor .....
7. Interest on loans, notes, mortgages, bonds, bank deposits, etc. .... 176.16

10. Rents .....	225.00	
11. Royalties .....	33,750.00	
12. * * *		
(c) Net gain (or loss) from sale or exchange of property other than capital assets. (From Schedule D) .....	(5,963.86)	
13. Dividends. (From Schedule E)		
14. Other income. (State nature)	67,484.74	
<hr/>		
15. Total income in items 3, and 6 to 14, inclusive.....		\$7,826,158.75

\* \* \*

[Endorsed]: Filed Oct. 11, 1955.

[Title of Tax Court and Cause.]

## FINDINGS OF FACTS AND OPINION

“Gross receipts,” for purposes of the excess profits tax “growth formula” (section 435 (e) (1), Internal Revenue Code of 1939) held to include all amounts received or accrued from sales, not excluding those added to the sales price as reimbursement for beer excise taxes.

VALENTINE BROOKES, ESQ., and  
RUSSEL SHEARER, ESQ.,

For the Petitioner.

AARON S. RESNIK, ESQ.,  
For the Respondent.



Respondent determined a deficiency of \$102,-343.94 in income and excess profits tax for the calendar year 1950, of which \$92,108.20 is in dispute. The single general issue involved is whether petitioner was entitled to compute its excess profits tax credit using average base period income under the alternative method based on growth, reflected by an increase in gross receipts. Resolution of that issue depends on whether the term "gross receipts" includes Federal and state beer excise taxes.

### Findings of Fact

Certain facts have been stipulated and are found accordingly.

Petitioner, a California corporation, brews and sells beer. It filed its returns for all years involved with the collector of internal revenue for the northern district of California. It keeps its books on an accrual basis and uses the calendar year. On January 1, 1949, petitioner changed its name from General Brewing Corporation.

Petitioner's base period was the calendar years 1946, 1947, 1948 and 1949. Adjusted basis for determining gain on sale or exchange of all assets held by it for business purposes as of January 1, 1946, amounted to less than \$20,000,000. It had no privilege of filing a consolidated return with any other corporations for 1950.

Petitioner reported on its income tax returns gross sales of \$12,878,751.99 for 1946, \$16,311,138.47

for 1947, \$18,161,135.39 for 1948, and \$23,003,696.22 for 1949. These amounts represent the total amounts received or accrued from the sale of beer. Federal and state excise taxes paid or accrued for 1946 through 1949 upon beer manufactured and sold totaled \$4,849,076.70, \$5,687,831.75, \$5,837,412.88, and \$7,192,289.27, respectively. These amounts were not excluded from gross sales but were included in cost of goods sold as reported on line 2 of the Federal income tax return.

The 2-year total of the gross sales shown on the 1948 and 1949 returns is \$41,164,831.61, and for 1946 and 1947 is \$29,189,890.46. The total for the later 2 years is 141 per cent of the total for the prior 2 years. The total of the gross sales, excluding Federal and state beer excise taxes, for 1948 and 1949 is \$28,135,129.46, and for 1946 and 1947 is \$18,652,982.01. This total for the later 2 years is 150.8 per cent of the total for the earlier years.

The following items also constituted gross receipts:

	1946	1947	1948	1949
Interest .....	\$ 768.88	\$ 749.99	\$ 4,284.73	\$ 1,360.56
Royalties .....	45,000.00	45,000.00	45,000.00	45,000.00
Sales of spent grain & sacks..	24,030.47	28,292.45	29,201.88	35,187.79
Sales of yeast....	3,476.61	4,755.06	7,670.25	11,747.47
Total .....	\$73,275.96	\$78,797.50	\$86,156.86	\$93,295.82

These items for 1948 and 1949 total \$179,452.68, and for 1946 and 1947, \$152,073.46. Those figures added to gross sales change the ratio including ex-

cise taxes from 141 to 140.9, and the ratio excluding taxes from 150.8 to 150.57.

Other income during the base period included:

	1946	1947	1948	1949
Cash discounts				
on purchases ..	\$11,642.97	\$26,314.59	\$27,108.96	\$43,530.23
Interest on. U. S.				
bonds .....	18,886.51	19,102.75	—	—
Judgment .....	—	3,139.88	—	—
Miscellaneous ....	1,071.96	41.13	—	25.45
Total .....	\$31,601.44	\$48,598.35	\$27,108.96	\$43,555.68

Inclusion of these amounts in the computations does not significantly affect the ratios of gross receipts.

On invoices covering shipments to customers within the United States, petitioner did not state beer excise taxes separate from unit prices. Invoices covering shipments to United States territories (e.g., Hawaii) stated that Federal tax was paid and the shipment was exempt from state tax. Invoices covering shipments to United States possessions (e.g., Samoa) stated that the shipment was tax-free.

During the years 1946 through 1949, petitioner published for various trading areas price schedules showing sale prices and terms. It regularly filed copies of schedules covering California areas with the California Board of Equalization pursuant to law. The California schedules did not state excise taxes separately. Price schedules for Nevada bore the notation that Nevada state tax was not included. Nevada schedules dated on and after February 1,

1948, specifically deducted California tax. The prices in Nevada from December 1, 1946, to February 1, 1948, were identical to those in Los Angeles from November 15, 1946, to June 20, 1947. Schedules for exports to United States possessions and foreign countries deducted both state and Federal taxes in the explanation of the price. Petitioner did not alter its methods of invoicing or pricing after March 1, 1950. It followed the general procedure in the brewing industry, not to show excise taxes separately on invoices or price lists.

Petitioner's published annual reports for 1946 through 1949 reported the same gross sales as shown on the returns. They did not show excise taxes separately.

Prior to March 1, 1950, breweries paid Federal excise tax by stamps. Petitioner carried the amount of unused stamps on hand, along with any state stamps, in an account entitled "Revenue Stamps on Hand." It carried this account as a separate item under "Current Assets" in the annual report, rather than as an inventory item. When beer was canned or bottled, it transferred the amount of stamps surrendered from "Revenue Stamps on Hand" to "Tax on Canned Beer" or "Tax on Bottled Beer." It paid state tax by monthly return on the previous month's sales.

Petitioner credited refunds to the "Tax on Bottled Beer" or "Tax on Canned Beer" accounts, except one substantially delayed refund in 1949, which it credited to "Miscellaneous Income."



After March 1, 1950, Federal tax was collected by stamp after the bottled or canned beer was withdrawn for sale or consumption. The beer tax statute remained unchanged during any material year.

Petitioner's accounts reflect manufacturing processes from the purchase of raw materials through the brewing, placement of beer in fermenting tanks, movement to aging tanks in cellars, and transfer to the bottling and canning lines. After packaging, beer is sent to the shipping warehouse and from there to distributors. "Inventory Beer in Process," to which a large bulk inventory is transferred when the beer reaches the cellars, reflects costs incurred up to that point including real and personal property taxes and social security taxes. After aging, the beer is withdrawn for bottling and canning, at which time costs of inventory in process are apportioned to a bottled beer cost account and a canned beer cost account, to which accounts bottling and canning costs are also charged. Warehousing and shipping costs are allocated to the bottled beer and canned beer cost accounts, which then show the total cost of beer produced exclusive of excise taxes.

Petitioner carried beer on hand in inventory. It recorded taxes paid on unshipped beer in accounts entitled "Inventory—Bottle Tanks—Federal Tax" and "Inventory—Canned Beer—Federal Tax." On the balance sheet it combined these accounts into "the inventory of federal tax," which in turn it combined with the bottled and canned beer cost accounts to arrive at a total inventory figure.

Since March 1, 1950, petitioner has used the same accounting method, except that it shows no Federal tax related to inventories, since it pays no tax until beer is sold. Its method of invoicing and pricing of merchandise remained unchanged. The tax now appears as an expense in the month when the liability accrues, as state excise taxes had always been handled.

Petitioner increased its over-all average prices, exclusive of excise taxes, for 1948 and 1949 over 1946 and 1947 by 21.6 per cent. Excise tax rates did not change during the base period.

No single classification of excise taxes is customary in accounting practice. Some are included in gross sales in corporate returns, while others are customarily excluded. Reports to stockholders generally conform to the company books, but may differ from the tax returns due to statutory requirements of tax reporting.

Where excise taxes are included in gross sales, tax returns and corporate reports subtract them as part of cost of goods sold, or as an expense deduction, or as a deduction from gross sales in arriving at net sales. Net sales for one period are frequently compared with those of another to determine a company's growth.

Petroleum companies exclude Federal and state gasoline taxes from gross sales. Retail establishments exclude state and city retail sales taxes, as

well as luxury taxes, such as on furs. The Federal tax on phonographs and television sets is customarily excluded. Those taxes are not regarded as an item of income or expense.

None of nine breweries chosen at random from Securities and Exchange Commission records excluded the excise taxes from gross sales, all reporting the total proceeds from beer sales. These breweries treated excise taxes in three different ways: Seven deducted the taxes from gross sales to arrive at net sales; another deducted both cost of goods sold and excise taxes from sales to determine gross profit; the ninth included excise taxes in cost of goods sold, dropping a footnote thereto stating that excise taxes of a certain amount were included.

A manufacturer makes no distinction as to excises on sales to a distributor or directly to the consumer.

Amounts of retail sales taxes collected, sometimes unknown, do not necessarily correspond to the amounts excluded from gross sales. California practice calls for application to the gross collections of a percentage based on an analysis of purchases as agreed to by the State Board of Equalization. Even though the retailer records the actual tax collected, he must apply the tax rate to his sales regardless of collections. Fractional differences in certain transactions necessarily result in an overage or shortage. Failure of collections to correspond to exclusions from gross sales does not improperly reflect income.



“Gross receipts” is not clearly or precisely defined by accountants, who usually keep accounts on the basis of “gross sales” and “net sales.”

Petitioner’s excess profits net income was overstated in the notice of deficiency by \$70,772.21 for 1949, but understated by that amount for 1948.

Petitioner’s gross receipts for the last half of the base period are less than 150 per cent of its gross receipts for the first half of its base period.

### Opinion

Opper, Judge:

Although a large part of the argument of the parties is occupied with an examination of the characteristics of the Federal and state tax on beer, we think the true issue requires a consideration primarily of the scope and purpose of the growth formula in the 1950 Excess Profits Tax Act.<sup>1</sup>

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<sup>1</sup>Sec. 435. Excess Profits Credit—Based on Income.

(e) Average Base Period Net Income—Alternative Based on Growth—

(1) Taxpayers to Which Subsection Applies—A taxpayer shall be entitled to the benefits of this subsection if the taxpayer commenced business before the end of its base period, and if either—

(A) (i) The total assets of the taxpayer as of the first day of its base period (when added to the total assets for such day of all corporations with which the taxpayer has the privilege under section 141 of filing a consolidated return for its first taxable year under this subchapter), determined under paragraph (3), did not exceed \$20,000,000, and

In place of the net taxable income test of the wartime excess profits tax law,<sup>2</sup> the statutory approach adopted in 1950 was to determine growth by presumably objective tests,<sup>3</sup> one of which was the size of the corporation's "gross receipts." The issue here is whether there should be considered as part of petitioner's gross receipts the amounts of Federal and state excise taxes on beer which it claims increased the selling price petitioner received for its product. If the amount of the beer taxes is excluded from gross receipts, petitioner's figures show an increment to more than 150 per cent, which entitles it to use the growth formula. If they are included in gross receipts the percentage falls some ten points lower and the growth formula is inapplicable.

The general approach of the 1950 Act was apparently an attempt to determine growth by an

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(ii) The total payroll of the taxpayer (as determined under paragraph (4)) for the last half of its base period is 130 per centum or more of its total payroll for the first half of its base period, or the gross receipts of the taxpayer (as determined under paragraph (5)) for the last half of its base period is 150 per centum or more of its gross receipts for the first half of its base period; or

\* \* \*

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<sup>2</sup>Sec. 713 (f), Internal Revenue Code of 1939 (Repealed by Sec. 122 (a), Revenue Act of 1945).

<sup>3</sup>See footnote 5 *infra*.

“increase” in “physical volume of production.”<sup>4</sup> Probably recognizing the difficulties of using that measure directly, the result was sought to be accomplished by the use of one of two “automatic”<sup>5</sup> tests: Either an increase of 30 per cent in payroll or an increase of 50 per cent in “gross receipts.” It is the meaning, and purpose of the use, of this term, which as to this issue is defined only as “The total amount received or accrued \* \* \* from the sale \* \* \* of stock in trade of the taxpayer \* \* \*”<sup>6</sup> which poses the instant question.

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4“\* \* \* The use of the alternative gross receipts test is justified by the fact that a corporation may increase its physical volume of production materially by introducing additional equipment and new operating procedures which do not involve a corresponding increase in its labor force \* \* \*” [H. Rept. No. 3142, 81st Cong., 2d Sess., p. 24; S. Rept. No. 2679, 81st Cong., 2d Sess., p. 27.]

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<sup>5</sup>Petitioner, in its brief, quotes as “relevant” two passages from the committee reports (H. Rept. No. 3142, *supra*, at pp. 16 and 17; S. Rept. No. 2679, *supra*, at p. 18), including the statements that tests applied under the wartime Act were “largely a matter of subjective judgment” and referring to the 1950 Act as providing “automatic formulas for each of the most important types of cases.” These statements were apparently made with reference to section 722. However, they may well represent the legislative frame of mind as applied to all the excess profits abnormality amendments.

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<sup>6</sup>Sec. 435. Excess Profits Credit—Based on Income.

(e) Average Base Period Net Income—Alternative Based on Growth—

Bearing in mind that it is an increase in physical volume of production with which the lawmakers were concerned, as petitioner apparently recognizes in its excellent brief, the question is what effect should be given to unit taxes, the rate of which did not increase during the base period. It can be accepted that percentage or ad valorem taxes would be neutral in such a situation since presumably they would increase in the same proportion as the total amount received from sales, at least unless the rate changed during the period. Similarly, a unit tax not based on any percentage of the selling price

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(5) Gross Receipts—As used in this subsection the term “gross receipts” with respect to any period means the sum of:

(A) The total amount received or accrued during such period from the sale, exchange, or other disposition of stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business, and

(B) The gross income, attributable to a trade or business regularly carried on by the taxpayer, received or accrued during such period excluding therefrom—

(i) Gross income derived from the sale, exchange, or other disposition of property;

(ii) Gross income derived from discharge of indebtedness of the taxpayer;

(iii) Dividends on stocks of corporations;

\* \* \*

and

(iv) Income attributable to recovery of bad debts.



would be neutral if the amount of the tax were increased during the base period in the same proportion that gross receipts increased. Petitioner's situation was different. It was subject to a unit, not an ad valorem, tax and the rate did not change during the base period but remained constant.

Neither the gross receipts test nor the payroll test, which is the alternative, are direct measures of physical volume of production. Gross receipts may rise at least in part due to an increase in the price of the commodity sold, as they did in the present case. Theoretically an increase of 50 per cent in the selling price might, without any addition to physical volume, create a statutory eligibility which was not actually intended. Similarly, a rise of 30 per cent in payroll might come about solely by an increase in wage rates with no improvement in physical volume. These possibilities were in the legislative mind but "the percentages used in the payroll and gross receipts tests" were deemed to be "sufficiently large so that only those taxpayers will be able to qualify whose business has grown substantially more rapidly than the average \* \* \*"<sup>7</sup> [Emphasis added.]

Petitioner suggests, we think correctly, that the tendency is to pass on to the consumer all possible costs of production. In ideal terms the growth formula will work best when all items of such costs, and, therefore, unit sales prices, remain static and any increase in gross receipts can hence be at-

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<sup>7</sup>S. Rept. No. 2679, *supra*, at p. 27.

tributed solely to a growth in physical volume. The test selected by Congress must assume that most production costs will remain stationary, otherwise the formula adopted by it would have no direct relationship to any increase in the physical volume of production. By that test items which remain stable in their relationship to units produced, such as the taxes in the present case, do not throw the formula off nor make its workings inequitable. Nothing less would compel a departure from the literal statutory language.

Petitioner is in effect asking that we reject a simple and direct application of the term "total amount received" as including everything received by the corporation in its own right, and employ instead a meaning which will give effect to the statutory purpose. We need not determine whether such an approach is permissible. Even if it were, it seems to us that the object of the statute as shown by its legislative history will best be served by including all items actually received and particularly those which represent a stable and unchanging cost per unit.

On this approach to the meaning of the Excess Profits Tax provision, it is of no consequence whether the beer taxes are manufacturers' taxes or sales taxes. They were included in the amount received for its stock in trade by petitioner, and we see nothing in the statute or its background which will justify their elimination. It is not contended

that such taxes, particularly the Federal tax,<sup>8</sup> are collected by the brewer as a trustee or fiduciary. While it may pass the economic burden of the tax to the purchaser, its failure to do so would not relieve it of the tax liability. *Lash's Products Co. v. United States*, 278 U.S. 175; *Liggett & Myers Co. v. United States*, 299 U.S. 383; *Shearer v. Commissioner* (C.A. 2), 48 F. 2d 552; *R. J. Reynolds Tobacco Co. v. Robertson* (C.A. 4), 94 F. 2d 167, certiorari denied 304 U.S. 563; *Casey Jones, Inc., v. Texas Textile Mills* (C.A. 5), 87 F. 2d 454; *Continental Baking Co. v. Suckow Milling Co.* (C.A. 7), 101 F. 2d 337; *Heckman & Co., v. I. S. Dawes & Son Co., Inc.* (C.A., D.C.), 12 F. 2d 154; *Consolidated Distributors v. City of Atlanta*, 193 Ga. 853, 20 S.E. 2d 421; *Western Lithograph Co. v. State Board of Equal.*, 11 Cal. 2d 156, 78 P. 2d 731; cf. *Indian Motorcycle Co. v. United States*, 283 U.S. 570; *Fresno Grape Products Corporation v. United States* (Ct. Cl., 1935), 11 F. Supp. 55; *F. Strauss & Son v. Coverdale*, 205 La. 903, 18 S. 2d 496; *Wayne County Produce Co. v. Duffy-Mott Co.*, 244 N.Y. 351, 155 N.E. 669. It cannot hence be said that amounts collected by petitioner, even though they effectively reimbursed it for the beer tax, were not its own "gross receipts."

Decision will be entered for the respondent.

Served July 19, 1956.

Filed and entered July 19, 1956.

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<sup>8</sup>If the Federal tax is not eliminated, petitioner would not qualify even disregarding the state tax.



The Tax Court of the United States, Washington

Docket No. 53063

LUCKY LAGER BREWING COMPANY, a Corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Findings of Fact and Opinion, filed July 19, 1956, it is

Ordered and Decided: That there is a deficiency in income and excess profits tax for the calendar year 1950 of \$102,343.94.

Entered July 23, 1956.

[Seal]     /s/ CLARENCE V. OPPER,  
Judge.

Served July 25, 1956.

Entered July 25, 1956.

In the United States Court of Appeals  
for the Ninth Circuit

Tax Court Docket No. 53063

LUCKY LAGER BREWING COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### PETITION FOR REVIEW

To the Honorable Judges of the United States  
Court of Appeals for the Ninth Circuit:

Lucky Lager Brewing Company, a California corporation with its principal office and place of business in San Francisco, California, petitions for review of the decision of The Tax Court of the United States entered on July 23, 1956, ordering and deciding that there is a deficiency in income and excess profits tax for the calendar year 1950 in the amount of \$102,343.94.

Petitioner's return for the year in question was filed with the Collector for the Northern District of California in San Francisco. Petitioner files this petition for review by the Court of Appeals for the Ninth Circuit pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code of 1939, and of Sections 7482 and 7483 of the Internal Revenue Code of 1954.

## Nature of the Controversy

The case presents a single question, whether federal and state excise taxes collected by petitioner from its customers and paid by it as taxes to the United States and the State of California are part of its "gross receipts" for the purposes of the excess profits tax growth formula provided by Section 435(e) of the Internal Revenue Code of 1939.

The amount of petitioner's excess profits tax for 1950 depends on whether or not it is entitled to compute its earned income credit as a growth corporation under the provisions of Section 435(e). Its eligibility for recognition as a growth corporation depends on whether its total "gross receipts" for 1948 and 1949 are 150 per cent or more of its total "gross receipts" for 1946 and 1947, as petitioner contends. The Tax Court held that that ratio was less than 150 per cent. If that determination is correct, petitioner is not eligible for taxation as a growth corporation.

The critical term "gross receipts" is defined by subdivision (5) of Section 435(e). The section defines gross receipts as "amounts received \* \* \* from the sale \* \* \* of stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer \* \* \* or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business, and the gross income attributable to a trade or business regularly carried on by the tax-

payer \* \* \*” The question is whether the amount of excise taxes imposed upon the manufacture and sale of each barrel of beer by taxpayer should be included in the term “gross receipts” as so defined. The Congressional history indicates that the section was intended to measure the taxpayer’s growth in terms of volume of physical production. There is no uniformity of accounting practice as to the meaning of the term “gross receipts”; some taxpayers excluding excise taxes from gross sales reported to stockholders and upon income tax returns; other taxpayers reporting gross receipts, deducting excise taxes to arrive at a figure of net sales. The only thing that can be said without hesitation is that there is no uniformity of treatment on income tax returns or reports to shareholders.

Petitioner’s practice in the base period, in common with that of most other breweries, was to include beer excise taxes in gross sales but also to include them in cost of goods sold, which is deducted before arriving at gross profit. However, the general practice in the petroleum industry, the phonograph and television sales industries, and the retail industry is to exclude excise taxes from gross sales, in consequence of which those excise taxes do not appear in their income tax returns, or corporate reports to stockholders, or profit and loss statements.

The beer excise taxes are a flat figure per unit, not a percentage of sales price, and were not in-

creased in the base period. If they are includible in a brewery's "gross receipts," then in order to qualify as a growth corporation a brewery must increase its units sales more than would another corporation subject to an excise tax imposed as a percentage of dollar volume, and more than would another corporation in an industry not accustomed to reporting excise tax collections in its gross sales; also more than a corporation in an industry where the excise tax was increased in the base period. The question is whether such a discrimination between industries by reason of difference in excise taxes and between taxpayers because of varying accounting and tax-reporting practices was intended by Congress when it imposed the excess profits tax, or whether a test uniform in its application to all industries was what was intended.

The Tax Court held that the definition of "gross receipts" compelled the conclusion that the non-uniform, discriminatory test was the one Congress intended to adopt. Petitioner contends that that determination is erroneous and that excise taxes collected on the sale of a product, including beer excise taxes, were intended to be excluded from the "gross receipts" by which growth is measured.

Dated: September 25, 1956.

Respectfully submitted,

/s/ VALENTINE BROOKES,

/s/ ARTHUR H. KENT,



/s/ PAUL E. ANDERSON,

/s/ RUSSEL SHEARER,

Attorneys for Petitioner on  
Review.

[Endorsed]: Filed Sept. 27, 1956, U.S.T.C.

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[Title of Court of Appeals and Cause.]

NOTICE OF FILING PETITION  
FOR REVIEW

To: The Honorable the Commissioner of Internal  
Revenue, Internal Revenue Service:

You Are Hereby Notified that Lucky Lager  
Brewing Company, a California corporation, did  
on the 27th day of September, 1956, file with the  
Clerk of The Tax Court of the United States, at  
Washington, D. C., a petition for review by the  
United States Court of Appeals for the Ninth Cir-  
cuit of the decision of The Tax Court entered on  
July 23, 1956, in the above-entitled case. A copy of  
the petition for review as filed is hereto attached  
and served on you.

Dated: September 25, 1956.

/s/ VALENTINE BROOKES,

/s/ ARTHUR H. KENT,

/s/ PAUL E. ANDERSON,

/s/ RUSSEL SHEARER,

Attorneys for Petitioner on  
Review.

ACKNOWLEDGMENT OF SERVICE OF NOTICE OF FILING PETITION FOR REVIEW

Service of the above and foregoing notice, together with a copy of the petition for review, is hereby acknowledged this 27th day of Sept., 1956.

/s/ JOHN POTTS BARNES,

C.W.R.

Chief Counsel, Internal Revenue Service, Attorney for Respondent on Review.

[Endorsed]: Filed Sept. 28, 1956, U.S.T.C.

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[Title of Court of Appeals and Cause.]

DESIGNATION OF THE RECORD ON REVIEW

Petitioner hereby designates the entire record in The Tax Court as the record on review.

Dated: September 25, 1956.

/s/ VALENTINE BROOKES,

A.H.K.

/s/ ARTHUR H. KENT,

/s/ PAUL E. ANDERSON,

/s/ RUSSEL SHEARER,

Attorneys for Petitioner on Review.



[Title of Court of Appeals and Cause.]

ACKNOWLEDGMENT OF SERVICE OF  
DESIGNATION OF THE RECORD ON RE-  
VIEW

Acknowledgment of service of a copy of the  
Designation of Record on Review is hereby made  
this 2nd day of October, 1956.

/s/ JOHN POTTS, BARNES,  
C.W.R.

Chief Counsel, Internal Revenue Service, Attorney  
for Respondent.

[Endorsed]: Filed Oct. 3, 1956, U.S.T.C.

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The Tax Court of the United States  
Docket No. 53,063

In the Matter of:

LUCKY LAGER BREWING COMPANY, a Cor-  
poration,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

Before: Honorable Clarence V. Opper, Judge.

Appearances:

VALENTINE BROOKES,  
RUSSEL SHEARER,

Appearing for the Petitioner.

A. S. RESNIK,

HONORABLE JOHN POTTS BARNES,

Chief Counsel, Bureau of Internal Revenue,

Appearing for the Respondent.

\* \* \*

FRED W. JORDAN

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Court: State your full name for the record.

The Witness: Fred W. Jordan.

Direct Examination

By Mr. Brookes:

Q. Where do you reside?

A. In Redwood City.

Q. What is your occupation?

A. I am the Treasurer and Comptroller for the Lucky Lager Brewing Company. [19\*]

Q. For how many years have you occupied those positions?

A. Since February 1, 1934.

Q. In that capacity, or in those capacities, what are your duties?

A. Well, I think the Comptroller is the main function I have in the brewery. I have charge of all the records of the company, and establish the accounting practice, with the help of our certified public accountants, and handle all finance matters for the corporation.

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\*Page numbering appearing at top of page of original Reporter's Transcript of Record.

(Testimony of Fred W. Jordan.)

Q. I hand you Petitioner's Exhibit 6, entitled "Flow Sheet of Accounting Entries from Books."

Did you prepare this? A. I did.

Q. Will you explain to the Court and for the record what this document constitutes?

A. Well, it gives in graphic form, I believe you would call it, the accounts that are carried on the books of the company and shows the process in manufacturing from the start of the purchase of the raw ingredient through the various phases of manufacturing, from the raw material through the brew house where the beer is brewed and gotten ready for cellar storage, where the beer is aged, and from there it is transferred to the bottling or the canning lines to be packaged into various sized bottles and cases. [20]

After the bottles are filled and packed, they are sent over to the warehouse, and from the warehouse are shipped out of the brewery.

The beer that remains on hand is carried in inventory.

Q. Will you explain the significance of the lines which appear by arrows on this exhibit?

A. Well, the first bracket takes in the raw material cost, and the brewhouse costs.

Mr. Resnik: When you are talking of the first bracket, is that over to the right?

The Witness: Yes. At that point the beer has been brewed, so to speak, and it is then transferred into the fermenting tanks and to the storage tanks and kept in the big storage tanks at the brewery until the beer is ready for bottling or canning.

(Testimony of Fred W. Jordan.)

As the beer comes to rest in the cellars, there is a large bulk inventory which at that time is transferred—as you can follow the arrow here—to inventory beer in process, and then when beer has to be made ready for bottling and canning, it is withdrawn from the storage tanks and goes through the bottling operations and canning operations.

When that phase of it has been completed, if you follow the arrow again, “bottling cost” goes to bottled beer cost, right opposite bottling cost. [21]

I should have mentioned earlier that the direct beer cost from the cellars is also—I am getting myself mixed up here.

The beer cost under the heading of “bottled beer cost” is transferred out of the beer in process inventory, and the bottling cost and canning cost, when those operations have been completed, are also transferred to bottled beer or canned beer cost.

There is one further phase, the warehousing and shipping cost, where the beer is kept in inventory until it is shipped out, delivered, or for sale, and that cost of warehousing and shipping is transferred to the same bottled beer and canned beer cost, the cost accounts, which give you the total cost of the beer produced exclusive of taxes.

Then when all costs have been gathered in that account, they are transferred to the bottle beer cost and canned beer cost, and at that time under the system that was then in effect, the bottle beer tax, or I should say the beer tax, was then paid by Government stamps. If there was bottled beer in in-

(Testimony of Fred W. Jordan.)

ventory, it had also a federal tax that was related to it that went in in the related account, either bottled beer or canned beer tax, and for the purposes of the balance sheet, the two accounts were then combined into an inventory of finished beer.

In other words, there was first inventory cost of [22] beer, and as we call it, the inventory of federal tax, and they were combined then to give an inventory of finished beer.

Q. (By Mr. Brookes): When you referred, as you did several times, to the word "tax" to what tax or taxes did you have reference?

A. To the federal excise tax on beer.

Q. Did you mean to include the state excise tax on beer? A. No.

Q. Was any treatment accorded to any excise tax on beer in Exhibit 6?

A. There is no state excise tax considered in this accounting at all. The state excise tax is only paid when the beer is sold or delivered.

Q. In this exhibit, in the three columns farthest to the right, as well as in the column labeled "bottling costs," and that labeled "canning cost," appear the word "taxes."

What taxes are referred to there?

A. Real and personal property taxes for the City and County of San Francisco.

Q. Has there been any change in the internal system of classifying accounts, changes from that exhibits, since the change in beer tax regulations in March of 1950?



(Testimony of Fred W. Jordan.)

A. There is no change in these accounts. The procedure [23] is the same. The only difference is that there is no federal tax now shown as being related to any beer inventories.

Mr. Brookes: Your Honor, it is a stipulated fact among the exhibits to the stipulation in which appears several samples of bills of this taxpayer to its customers, and from which appears the stipulated facts that where the tax was due, it was not set forth as a separate item of charge on the billing to the customer.

I wish your Honor to know that because it is the premise of the next question I shall ask the witness.

Q. (By Mr. Brookes): Mr. Jordan, do you know why the company did not show the tax separately in its billing to its customers?

A. Only to the extent that it was a general procedure in all the brewing industry. They all showed their invoices with the total amount including both cost of beer and the federal tax and the state tax as well.

Mr. Resnik: I want to have your question clarified as to whether it included both federal and state taxes, but the answer stated that.

Q. (By Mr. Brookes): Do you know the reason for this custom in the beer industry?

A. No, I really don't. As far as I know, it has always been that way. [24]

Q. Do you know the reason that Lucky Lager followed this practice?

(Testimony of Fred W. Jordan.)

A. We had to be competitive, and I would say that we did the same as the others, and when we first started selling, the others were already in business and we followed, in a sense, their method of procedure.

Mr. Brookes: Before passing on, I should like to call your attention to the fact that among the stipulated exhibits are some in which sales have been made which were not subject to tax, not subject to state tax, or in some instances, not subject to the federal tax, by reason of being sales in export—in those instances the stipulated exhibits show a deduction of the tax, and a specification of what tax is being deducted in arriving at the final selling price.

That being stipulated, I shan't go into it with this witness.

Q. (By Mr. Brookes): Mr. Jordan, I hand you Stipulated Exhibit No. 2, Roman II. There is a lateral column entitled, "Discounts Received."

Will you please explain what the discounts received were?

Mr. Resnik: If your Honor please, I would refer the Court to the stipulation and would point out to the Court [25] that any inquiry as to that item is completely meaningless since its inclusion or exclusion from gross receipts, or partial inclusion or partial exclusion from gross receipts can't vary the formula. The taxpayer will either win the case with the beer tax in or out, and we would just make



(Testimony of Fred W. Jordan.)

a lot of progress if we could just dispose of those items which cannot affect the issue at all.

Mr. Brookes: I think the witness could have answered the question in the time it took Mr. Resnik to state his objection, and he could answer the next question in the time that it will take me to answer his objection.

It is true, as I stated in my opening statement, that the result of the case is not going to be affected one way or the other by the mathematics on any determination made by the other items. We are not in agreement with the Government about the classification of that item, or the next one, and others, but we put them in issue and they are in issue in the pleadings, which are part of the record in this case.

In order that there be no adverse or possible adverse implication drawn from our failure to state the reason for our objection to the classification that the Government has insisted upon in the case, I wish to have the witness testify as to the nature of these items, the figures of which are set forth in the stipulation. [26]

Mr. Resnik: It is because of what Mr. Brookes stated that I made my earlier statement to the Court. In view of the fact that some of the small items which are incorporated in the exhibit to the stipulation can't vary the result of the case, we had intended not to pursue it, and we would ask the Court, we would join with Mr. Brookes in asking

(Testimony of Fred W. Jordan.)

the Court that no inference should be drawn for one side or the other as to the inclusion or exclusion of any of those minor items.

What we have proposed at the outset was an attempt to get the case down to the nub, to the heart of the case, and we thought we might do that on a give and take basis.

We couldn't come to a final agreement, and we realized ultimately that it wasn't necessary to come to final agreement on a give or take basis, and for that reason some items are included, and if they were material in another case, no one knows what position might be taken, so I would ask the Court, even if the witness were permitted to testify, not to draw any inferences favorable or unfavorable therefrom.

The Court: I am not going to sustain the objection.

Mr. Brookes: This will be very brief.

The Court: Proceed.

Mr. Brookes: Will you read the question, Mr. Reporter, please?

(Question read.) [27]

The Witness: The discount received consists of the usual one or two per cent that you get from payment, either in 10 days or 30 days, or whatever the terms may have been. We have taken that in as discounts received on the record as income.

Q. (By Mr. Brookes): Mr. Jordan, Exhibit 2

(Testimony of Fred W. Jordan.)

has another column entitled "Interest on U.S. Bonds," in which figures appear for the years 1946 and '47, and none for 1948 and '49.

What was the reason that the taxpayer owned United States bonds in 1946 and '47?

A. The reason we owned those bonds was that the brewery then contemplated building another brewery in Azusa, Los Angeles County, and the money was used to purchase these bonds. When the time came that we were able to build, or got permission to build, these bonds were then cashed in and used for the building purposes, or the purchase of the land.

Q. Do you know whether or not there were price increases in the taxpayer's product during all the years 1946 to '49, inclusive?

A. Yes, there were.

Q. Do you know what those price increases amounted to?

A. 21.6 per cent, the over-all average increase for both bottled and canned beer. That is exclusive of the federal and state tax. [28]

Mr. Resnik: May I have the reporter read the answer to the last question?

(Answer read.)

Q. (By Mr. Brookes): For what period was that calculated?

A. For the 1946 and '47, as compared to the years 1948 through '49.

Mr. Brookes: Thank you. You may cross-examine.

(Testimony of Fred W. Jordan.)

Cross-Examination

By Mr. Resnik:

Q. Mr. Jordan, you just testified as to an increase in prices. Doesn't your company have a different price for the same product in different areas in the state of California? A. At this time?

Q. The years '46 to '49. That is the critical period in this case.

A. I don't recall. I think there were different prices at that time. I wouldn't be sure.

Q. Different prices for different areas?

A. That is right.

Q. And you had still different prices for the state of Nevada? A. Yes.

Q. So that when you stated that the prices increased 21 per cent, of what prices were you speaking? [29]

A. The total sales that were made throughout any area, exclusive of federal and state taxes.

Q. Do you mean that the prices in the Imperial area increased 21 per cent in the period?

A. No; the over-all average, whether it was in Nevada or Southern California or Utah, the price increase of the product was 21.6 per cent, exclusive of federal or state taxes.

Q. So in actuality, the price increase in Nevada might have been more or less than that?

A. It could have been, yes.

Q. You are merely talking of an average now?

A. Yes.

(Testimony of Fred W. Jordan.)

Q. Actually, the price that you get for beer is determined by many factors, is it not?

A. In what way?

Q. Doesn't competition set in to assist in the establishment of price?

A. Well, to meet competition, yes.

Q. Competition from other brewers?

A. Yes.

Q. Competition from other soft drinks?

A. I don't know.

Q. Competition from hard liquors and wines?

A. I don't know as to that; probably, yes. [30]

Q. Are you in that department of Lucky Lager Brewing which is concerned with the establishment and maintenance of prices?

A. Of determining prices for sale?

Q. Yes.           A. No.

Q. You stated, Mr. Jordan, with reference to Exhibit 6, that personal property taxes on the beer appeared in some column. Will you explain that to us?

A. Brew house taxes, those represent real and personal property taxes.

Q. Isn't it a fact that in personal property taxes levied by the City and County of San Francisco, that you pay a personal property tax on the beer in the vat before it goes through the meter?

A. Whatever is in inventory, yes.

Q. And the tax on that is at a different rate than the tax on the beer after it has gone through the meter and the federal excise tax has been paid?



(Testimony of Fred W. Jordan.)

A. Would you state that again, please?

Q. Do you know how the personal property tax for the City and County of San Francisco is levied on the brewer?

A. Yes; we issue a report each year.

Q. Give them a report of the beer in the vats, don't you? [31] A. Yes.

Q. And they assess a certain tax on that, generally based upon cost? A. That is right.

Q. And the cost upon the beer in the vat is cost less the federal beer tax, is it not?

A. That is right.

Q. Did you say you haven't paid the federal beer tax? A. That is right.

Q. But once that beer went through the meter, before it went into the bottling house in the period 1946 to '49, the federal tax became due, did it not?

A. As it went through the meter, yes.

Q. So when the personal property tax was assessed on the beer, it had passed through the meter, they determine the tax on a cost inclusive of the federal tax, do they not?

A. I suppose they did. I don't know their exact method of evaluating it.

Q. Now, then, referring again to Exhibit 6, can you tell us where on that exhibit the state beverage tax appears? A. State beverage tax?

Q. Yes.

A. There is no state beverage tax in any of these accounts. That tax did not apply until the sale or delivery was made. [32]



(Testimony of Fred W. Jordan.)

Q. I show you an exhibit attached to the stipulation which I believe to be Roman number V, the first sheet of which is entitled, "Account No. 93, Sheet No. 1, Operating Ledger, State Beverage Tax Payable."

A. That is right.

Q. Referring to that sheet, we see thereon in the first block, that some portion of the state beverage tax went to bottled beer cost of sale?

A. Right.

Q. Part of it went to canned beer?

A. Right.

Q. Where do the legends comparable to the legend "Bottled Beer Cost of Sales" and "Canned Beer" appear on Exhibit 6?

A. They do not appear on this exhibit. They appear on the income and expense statement. They are charged to the income or expense in the month in which that tax liability is accrued, and this represents the liability which was usually paid in 15 or 30 days later.

Q. So Exhibit 6, although denominated a flow sheet of accounting entries, from the books of Lucky Lager, is incomplete, is it not?

A. Well, this is a manufacturing flow of accounts, and the ultimate conversion of all the materials and the labor into inventory. The state tax only applies when that [33] beer is taken out of inventory and sold.

Q. Or delivered? A. Yes.

Q. Where do your federal social security taxes appear on Exhibit 6?

(Testimony of Fred W. Jordan.)

A. You find those on about the fifth row from the bottom. They are all labeled "social security taxes."

Q. Referring again to Exhibit No. 5, the beverage taxes table, notwithstanding that the state beverage taxes payable do not appear on Exhibit 6. Nevertheless the state beverage taxes are a charge to the cost of beer sold, are they not?

A. That is the way we treated it on the records, yes.

Q. Mr. Jordan, with reference to the federal excise taxes, particular during the period here material, the years 1946 to 1949, if any of the beer was destroyed after it left the bottling house, not before, but after it left the bottling house, there was no opportunity for recovery of that tax, was there?

A. Are you speaking of the period 1946 through '49?

Q. Yes.

A. In the event, when you say "after it left the bottling house," do you mean it got outside the brewery premises?

Q. Yes. [34]

A. There was no refund then.

Q. At one time there was a change in the law, however, to give you some allowance for spillage within the bottling house? A. Yes.

Q. And after March of 1950, there was a further change as to the time when you could pay your tax? The bottling house was then brought upon the bonded premises, is that not the case?

(Testimony of Fred W. Jordan.)

A. That was March 1, 1950. The tax was still paid by stamp, but it was only paid on that packaged merchandise which left the brewery premises.

Q. What about the beer that left the bottling house but was not delivered for consumption or sold, but was just stored? That was stored tax paid, was it not?

A. During the 1946 through 1949 period.

Q. And even after March 1 of 1950?

A. No, not after March 1, 1950, because the tax only applied after the beer was delivered or sold.

Q. Let me see if we can make the question clear. Let's take the period after March 1 of 1950.

A. Yes.

Q. The beer has gotten into the bottling house and is bottled? A. Yes. [35]

Q. It then passes along a moving line, past some electronic counters, which counters are there for the purpose of determining how much tax has to be paid and the tax is then paid, is it not?

A. Not at that time. March 1, 1950, changed the manner of tax payment. The beer was still paid by stamp, but the stamps were not cancelled until the beer had actually moved off the bonded premises.

Q. Moved off the bonded premises, but it could still move into a warehouse and remain unsold, could it not?

A. In our own warehouse on bonded premises. All our premises were bonded. We did not pay any tax.

(Testimony of Fred W. Jordan.)

Q. Did you ever maintain an inventory of finished beer?

A. Outside of the brewery premises?

Q. Yes.

A. Not to my recollection during those years.

Q. What about the inventory on the brewery premises?

A. There would be no need for—there would be no federal tax paid on them. It was in inventory and the stamps, as I say, the payment did not have to be made until the beer was delivered.

Q. But prior to March 1 of 1950, and during all the period here material, the tax was paid on the beer even before it reached the bottling house; is that correct? [36]

A. It was paid when it got into the bottling house tanks, when it was transferred from the cellars and put into the bottling tanks, and the tax was then paid, or we had stamps on hand to cover it.

Q. In fact, there was a meter just outside the bottling house which checked the amount of beer that flowed through, and at that point of time the tax was paid?

A. That is right; that is March 1, 1950.

Q. Directing your attention to Roman Exhibit III, to the stipulation, these being invoices of Lucky Lager Brewing Company, and directing your attention to an invoice of beer shipped to Sacramento, California, what unit price of \$2.56 was indicated thereon—that price of \$2.56 includes not only the federal excise tax but the state tax as well?

(Testimony of Fred W. Jordan.)

A. That is correct.

Mr. Resnik: No further questions.

Redirect Examination

By Mr. Brookes:

Q. Did you testify that this flow sheet, Exhibit No. 6, is a statement of the accounts as they appeared during the years 1946 to 1949, inclusive?

A. Were they in this manner?

Q. Yes.           A. Yes.

Q. If a flow sheet similar to this were [37] prepared, showing the way in which the accounts were maintained in 1951, for example, or any period after March 1, 1950, would there have been any figures or any names or identification representing the federal beer tax?

A. Speaking of 1950 now?

Q. After the change in March of 1950?

A. The beer tanks then would have been the same, handled in the same manner; that is, recording the state excise tax, because then it applied on delivery, and these accounts that are here shown, the inventory of bottled beer, federal tax and canned beer federal tax, none of them would appear.

Q. You testified, Mr. Jordan, as to the way and time at which the federal beer tax was paid in the base period, 1946 to 1949, and prior to the change in March of 1950, and that the tax was paid at the time that the beer was withdrawn from tanks and placed in containers for sale.



(Testimony of Fred W. Jordan.)

Was there any provision under which the company could get refunds in the event of spillage, breakage, or anything of that nature, after the bottling?

A. Again, this is the base period?

Q. Yes.

A. Yes. If we set aside short fills or foreign matter might have got into the bottles, those were set aside. Then under the practice, we would ask the Alcohol Tax Unit at that [38] time for an inspector to come out and witness the destruction of that beer, under his supervision. He would determine how much gallonage or barrels we had there and refund the tax, based on the barrelage that was destroyed or dumped down the sewer.

Mr. Brookes: That is all.

### Recross-Examination

By Mr. Resnik:

Q. After March 1, 1950, you stated that the federal beer tax would not have appeared on Exhibit 6?

A. Right.

Q. Would it not have been handled in the same manner as the state beverage tax was handled prior thereto and still be reflected as a charge against cost of sales?

A. No; it was reflected differently. We were still required to buy federal stamps, the same as we did in the years before. The only difference was in the method of collecting that tax. In the base period, the beer was metered and we have to pay on the



(Testimony of Fred W. Jordan.)

meter, whatever the meter showed. After that, March 1, 1950, the tax was paid with the stamps, but only on the beer that left the premises. Therein lay the difference.

Under the prior method we had to pay it regardless, on the meter reading. After March 1, 1950, we paid it on the beer that was actually bottled in containers and was delivered [39] or sold and left the plant.

Q. How was the federal tax recorded on your books of accounts after March 1, 1950?

A. First of all, the revenue stamps were purchased and it was charged to revenue stamps on hand. Then each day, or the next following day after operations, the tax was determined that was due and payable on the shipments and sales that had been made on the prior days, and the equivalent in federal excise tax stamps was cancelled and sent down to the customs collector, or whoever it was.

Q. Did that charge find its way into your cost of goods sold?

A. At that time it had the same treatment, or showed up in the accounts then in the same manner that the state excise tax showed. It became a deduction directly from income. It never went into any inventory.

Q. So that it did finally wind up as an inclusion in cost of goods sold?

A. That is right.

Mr. Resnik: No further questions.

Mr. Brookes: That is all.

(Witness excused.)

Mr. Brookes: By way of explanation, it is a stipulated fact, and for that reason I asked no questions of this witness on the point—the federal beer stamps on [40] hand during the base period purchased but not affixed or destroyed or mutilated were, according to the stipulation of facts, not carried as an item in inventory, but were carried in the balance sheet as a separate classification, separate heading under “General Classification—Current Assets.”

I should like to call for examination Mr. Walter M. Baird.

Whereupon

WALTER M. BAIRD

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

The Clerk: Will you state your name, please?

The Witness: Walter M. Baird.

Direct Examination

By Mr. Brookes:

Q. What is your address?

A. My business address is 120 Montgomery Street.

Q. What is your occupation?

A. Certified Public Accountant.

Q. How long have you been a certified public accountant?

A. I have been certified for 16 years.

Q. And have you practiced accountancy longer than that? [41]

A. For 19 years.

(Testimony of Walter M. Baird.)

Q. Have you a professional association with an accounting firm? A. Yes.

Q. What is the firm?

A. Price, Waterhouse and Company.

Q. What is your position with that firm?

A. I am a partner.

Q. What are your duties with that firm?

A. I, together with my other partners in San Francisco, have general supervision over the work done by our San Francisco office for our clients, which includes the audit of their financial statements, general accounts, and accounting tax accounting advice, and other advice to our clients as is normally associated with offices of certified public accountants.

Q. Does your firm have offices in other cities?

A. Yes.

Q. How many in the United States, Mr. Baird?

A. About 30.

Q. How many national partners does the firm have?

A. 61, including two outside of the United States.

Q. Does that include you? A. Yes.

Q. Does your San Francisco office have any clients [42] which are subject to state and federal excise taxes? A. Yes.

Q. Have you worked on the accounts of such clients? A. Yes.

Q. Do you know how such excise taxes are customarily classified in accounting practice?

(Testimony of Walter M. Baird.)

Mr. Resnik: I object, your Honor, until we have a specification of the particular type of tax and the company we are concerned with. Otherwise the answer would be completely meaningless and the question is too broad and not relevant to the issue in this proceeding.

Mr. Brookes: I think this witness has been shown to be an expert on accounting practices and accounting customs and matters of accounting generally. It is true that I didn't ask him which excise taxes were customarily classified in which way. Perhaps that will come out in the answer to the question.

I have been careful, perhaps too careful, not to be appearing to lead this witness, and I have no objection to specifying the excise taxes about which I should like an answer, if I can be assured that I won't then be faced with the objection that I was leading the witness.

Mr. Resnik: We haven't even established that this witness is familiar with the brewing industry or that he is the accountant for Lucky Lager. [43]

Mr. Brookes: I will ask him if their firm is the accounting firm for Lucky Lager Brewing Company, the taxpayer in this case.

The Witness: Yes.

Q. (By Mr. Brookes): Are you familiar with the account of that client? A. Yes.

Q. When you stated that your San Francisco office has clients which are subject to state and

(Testimony of Walter M. Baird.)

federal taxes, were you referring, among others, to Lucky Lager Brewing Company?      A. Yes.

Q. And when you stated you had worked on the account of such clients, were you including Lucky Lager Brewing Company?      A. Yes.

Q. Were you also including corporations engaged in the petroleum industry and selling refined petroleum products?      A. Yes.

Q. Were you also including corporations that were engaged in selling at retail, such as department stores?      A. Yes.

Q. Is there another type of client subject to federal and state excise taxes that should be added to that list on whose affairs you have worked?

A. We mentioned oil companies and department stores. [44] I might mention grocery stores as another type of retail establishment. Those are all I can recall at the moment. I think I am familiar with some practices in other industries.

Q. Do you know whether all excise taxes are customarily classified in accounting practice in the same way?

Mr. Resnik: I object, your Honor. I don't believe we have any issue in this proceeding requiring the testimony of an expert accountant as to how other excise taxes may be classified by other taxpayers in relation to other problems. We have here a narrow issue of the determination of gross receipts by a specific taxpayer under the specific facts here in issue under a specific statutory provision levying the tax upon beer.



(Testimony of Walter M. Baird.)

The Court: Overruled.

Mr. Brookes: Mr. Reporter, will you read the question to the witness?

(Question read.)

The Witness: They are not.

Q. (By Mr. Brookes): Is the accounting practice to include some excise taxes in gross sales in the ordinary——

Mr. Resnik: I object.

Mr. Brookes: May I finish the question?

Q. (By Mr. Brookes): ——in the ordinary corporate income tax return? [45]

Mr. Resnik: I object on the same ground as before mentioned. If I can have a continuing objection to the line of questioning——

The Court: You will have to make your objection each time because I won't know when it is going to end.

Overruled.

The Witness: Different excise taxes are treated differently.

Q. (By Mr. Brookes): My question was whether it was accounting practice to include certain excise taxes in gross sales in the ordinary corporate income tax return?

A. Some excise taxes are included in gross sales in corporate income tax returns; some excise taxes are customarily by trade practice excluded from gross sales in corporate income tax returns.



(Testimony of Walter M. Baird.)

Q. When some are included and some are excluded from gross sales in the corporate income tax returns, would similar practice of inclusion or exclusion be followed in reports to stockholders or other reports that are made in general accounting practice under regularly accepted accounting customs and practices?

Mr. Resnik: I object, your Honor. I don't see how that has any materiality to the issue in this case. The question is broad, not even related to a particular type of business or enterprise and wouldn't have any connection with [46] this taxpayer whatsoever, nor has there been any specification of a period of time or the nature of the tax being discussed.

The Court: Overruled.

Q. (By Mr. Brookes): Which excise tax—excuse me.

A. It would be usual for the reports to stockholders to be prepared in the same manner.

Q. Mr. Baird, which excise taxes are customarily excluded from gross sales in these reports?

A. It is customary for petroleum companies to exclude their excise taxes. It is customary for retail establishments to exclude the retail sales tax, both state and city. It is customary for retail establishments to exclude so-called luxury taxes, such as furs. It is customary in the amusement business to exclude the admissions tax from revenues. It is customary to exclude the excise tax on phonographs and television sets from gross sales.

(Testimony of Walter M. Baird.)

Q. Mr. Baird, that is a federal excise tax to which you last referred, is it not? A. Yes.

Q. And when you referred to the excise tax on the petroleum industry, were you referring to both federal and state excise taxes? A. Yes.

Q. And how are those excise taxes treated which are [47] not excluded from gross sales?

A. They do not appear in either sales or expenses. They are excluded from both in any report.

Q. But I meant to ask about those excise taxes which are not among those which are excluded from gross sales; wherein and how do they appear in the tax returns and in the corporate reports?

A. They will appear in different ways. They may appear as part of the cost of goods sold. They may appear as a separate deduction from the gross sales to arrive at a net sale, which is the case that is often found, in order to arrive at net sales, which is the usual test that is given in a comparison of the company's growth.

They may appear in the tax return as an item of tax, so-called, "below-the-line" deduction. I have even seen it appear on Line 1 as a separate deduction from sales; as you know the Line 1 setup on the tax return. Therein the taxpayer had to write in the word "taxes" because it isn't provided for in the form.

Those are various places it occurred and how they are treated.

Q. Do you know how the federal and state excise

(Testimony of Walter M. Baird.)

taxes have been treated by Lucky Lager Brewing Company?      A. Yes.

Q. And do you know how those federal and state excise [48] taxes have been treated by other leading brewers in 1946, the first of the years with which we are concerned, and subsequently?

A. Yes. Your Honor, may I refer to a memorandum to refresh myself as to numbers, here?

Mr. Resnik: May I see the memorandum, please?

The Witness: Yes.

Mr. Resnik: May I have the witness on voir dire, if he is going to refer to it?

The Court: It is not being offered as an exhibit.

The Witness: I had a summary made for me of nine breweries which filed financial statements with the Securities and Exchange Commission for 1946.

Q. (By Mr. Brookes): And later years?

A. Through 1954, as a matter of fact.

Of those six in 1946, and seven in all other years, through 1954, in their profit and loss statement included in Form 10-K, Securities and Exchange Commission, treated the state and federal excise taxes as a separate deduction from gross sales to arrive at net sales.

Q. How were the others treated, Mr. Baird?

A. One of the others included the taxes in gross sales and showed as a deduction from gross sales to arrive at a figure of gross profit, the sum of two items, one entitled [49] "Cost of Goods Sold, or

(Testimony of Walter M. Baird.)

Product Sold," and two, "State and Federal Excise Taxes."

The ninth one included the excise taxes in gross sales and included the excise taxes; the debit in cost of goods sold, and a footnote thereto stating that it included excise taxes of "X" dollars.

Q. In which of those categories does the system of classification of accounts fall which is similar to that which Lucky Lager uses?

A. The final one I described.

Q. As a matter of accounting theory, is any one method to be preferred over any other method?

Mr. Resnik: If your Honor please, I object. I don't believe we have any issue here with reference to a better or poorer method of accounting procedure. We have an issue arising of a provision of the Internal Revenue Code which this Court will construe, and any construction given it by a certified public accountant can't advance its meaning insofar as the issue in this case is concerned.

I submit the question is irrelevant, incompetent to any issue in the proceeding.

The Court: Overruled.

Mr. Brookes: Would you read the question to the witness?

(Question read.) [50]

The Witness: The survey produced three different results. In nine breweries, all of which filed Securities and Exchange Commission reports, all of those financial statements had to have been re-

(Testimony of Walter M. Baird.)

ported upon by independent public accountants. Therefore, it would appear that any of them is acceptable accounting treatment.

However, I am very much impressed by the fact that 7 out of the 9 treated it in one manner.

Q. (By Mr. Brookes): Mr. Baird, you testified previously that the sales tax, the state sales taxes in California, I presume, and the federal and state gasoline distributors' taxes, and others that you enumerated, were examples of excise taxes which, under customary accounting practice, are excluded from gross sales in taxes on other corporate reporting.

Are they excluded from gross sales as regularly when the product is sold first to a distributor by the manufacturer or taxpayer, and then sold by the distributor to the consumer, as they are when the product is sold by the manufacturer directly to the consumer?

A. There is no distinction made as to who the buyer was.

Q. Did I understand you to testify that in the case of sales taxes in California, and the city sales taxes in California, that these sales taxes are excluded from gross [51] sales in corporate reporting?

A. Yes.

Q. Do the collections of sales taxes by retailers actually correspond to the amount excluded from gross sales in these reports?

A. Not necessarily; sometimes the amount collected isn't even known.



(Testimony of Walter M. Baird.)

Q. Why is there no correspondence between collections and the excluded amount?

A. As an example a chain grocer whose sales include not only taxable items, but not taxable, may well not keep track of the taxable items, and the non-taxable items that he sells, but when it becomes necessary for him to file his tax return, he takes his collections, which would include both the amount to which the products are sold and the taxes that he did collect from his customers, and he applies a percentage to that, which is a percentage agreed upon with the State Board of Equalization as to the proportion of his sales which should be considered to be taxable, and those which should be considered to be non-taxable.

That percentage is arrived at by an analysis of purchases. That percentage has been applied to his total collections, which will then give the assumed taxable sale, 3 per cent, that is thereby computed, and that is the amount he pays to the state government for his retail sales. [52]

Q. Is this confined to the instances of grocery stores, or does it apply in the case of department stores or other retailers as well?

A. It applies to a case even where those establishments do keep track of the actual amounts of tax they collect from the customer; they are obligated to pay to the state three per cent of their sales whether or not they have collected it from the customer. There is always an overage or shortage.



(Testimony of Walter M. Baird.)

Q. Why is that?

A. For example, on a 15 cent purchase in the state of California, you pay one cent sales tax, where actually three per cent is only .45 of one cent, thereby the store collects .55 of a cent too much. On \$1.10 it is 3.00, so there is always a plus or minus.

Q. Does this non-correspondence of collections with amounts excluded from gross sales in the case of these retailers result in any improper reflection of net income?

A. Not a bit; it has no effect on net income.

The Court: Let's take a recess.

(Short recess taken.)

The Court: Proceed.

#### Cross-Examination

By Mr. Resnik:

Q. You testified that some analysis was made for you [53] of the method of treatment of federal and state beer taxes by nine breweries. In each of those nine cases what source of information was used?

A. Form 10-K, filed with the Securities and Exchange Commission.

Q. It wasn't a federal income tax return?

A. No.

Q. In each of those instances, did you not find

(Testimony of Walter M. Baird.)

that the figure of gross sales which appeared thereon included the federal and state beer taxes?

A. It did, except that in one case of Krueger in 1946, which is parenthetically noted.

Q. Wasn't that stated as follows: "Income from sales net after returns and allowances and less federal and state excise taxes"——

A. I think that is what it said. May I look at my copy now?

Q. Yes. A. Yes, you are correct.

Q. You testified that it is not unusual for reports to stockholders, or perhaps even other certified statements, to be at variance with the method of reporting income receipts and deductions for tax purposes; is that correct? A. Not exactly.

Q. Let me ask you this: Doesn't it occur with some [54] degree of frequency that companies will publish statements to stockholders, make statements to banks, or to other interested parties on a basis that are variance with the method of reporting for federal tax purposes?

A. I should like to answer that this way: The taxable income is not necessarily reported income.

Q. So that statements to stockholders could and sometimes are prepared on bases different from the accounting for tax purposes?

A. I can say that this reporting to stockholders is necessarily in agreement with the company's books, and the only variations from that would be the particular statutory differences provided for in the income tax accounts, which are contrary to gen-

(Testimony of Walter M. Baird.)

eral accepted accounting principles where the tax law is wrong.

Q. Well, Commissioner Andrews might want to correct that.

A. Well, Congress tried to last year and didn't get very far.

Q. Does your company represent any other local brewers?           A. No.

Q. Does your company represent any other brewers throughout the country?

A. Yes. [55]

Q. What brewers do you represent?

A. The only ones that come to my attention—I haven't made a study of this—is Pabst.

Q. Did you see their tax returns for the period here material?           A. No, I have not.

Q. Were you able to ascertain how Pabst reported its gross receipts?

Mr. Brookes: Your Honor, I have to object to Mr. Resnik's attempting to bring out information which is confidential in nature with respect to Mr. Baird's clients, whom he has seen fit to ask Mr. Baird to name, other than this taxpayer. Mr. Baird's testimony has been in terms of customary practice, except to the extent that names and figures would appear from published reports in the Securities and Exchange Commission, and I don't believe it is relevant. Therefore, it isn't necessary to cause a violation of confidential relationship, which accountants and auditors have to their clients to require that there be a disclosure of the names of particular

(Testimony of Walter M. Baird.)

clients of Mr. Baird's firm, and their policies, particularly in respect to their tax purposes, as to which there is a secrecy statute that would keep us from producing the tax returns, if we could get them.

Mr. Resnik: I know of no privilege between client and accountant that prevails in the tax court, your Honor. [56]

Mr. Brookes: I was not speaking of technical legal privilege. I recognize there is none.

The Court: I think this is something that can be claimed only by the witness. Had I known there would be any question of not going into details, I would have sustained the objection when it was made in the first place.

I don't see how a witness can be allowed to testify generally, and the minute he is asked to go into details so they can be checked and verified, he hides behind some sort of privilege.

Mr. Brookes: Your Honor, he can't, but I do believe that Mr. Baird has disclosed to Mr. Resnik the information from which he testified, which was on the sheet he carried in his pocket.

In addition to that, he testified that there was one taxpayer whom he knew of from his experience who included on his tax return that Mr. Baird had seen, in the first line, the deduction from sales in arriving at net sales for the figure of federal excise taxes.

Certainly I concede Mr. Resnik is entitled to go into that. I think he will find it was not Pabst. He

(Testimony of Walter M. Baird.)

is asking him about details on which I think Mr. Baird did not base any of his general testimony.

The Court: I think you asked Mr. Baird questions about whether he represented brewers, people in the field of [57] paying excise tax. He said he did, and then some general questions were based upon his experience in that field. My recollection is that there was an objection made and I overruled it.

I am not going to sustain your objection at this point, unless you are willing to withdraw that line of questioning.

Mr. Brookes: Your Honor, I believe my line of questions was permissible.

The Court: I think it was, too.

Mr. Brooks: I can't withdraw it, your Honor. In that event, I think I will have to stand on the objection and if your Honor sees fit to overrule it, I shall sit down promptly.

The Court: Overruled.

The Witness: The question is how Pabst treated that?

Q. (By Mr. Resnik): Yes.

A. It is my recollection in the published accounts—and I have never visited their offices nor seen their books or worked on their accounts—that they have treated that the same way that Fort Pitt Brewing Company has done in their statement, which was including it in gross sales and cost and expenses. [58]

Q. Do you know of any brewer who did not include in gross sales the total proceeds he received



(Testimony of Walter M. Baird.)

for his beer?           A. No.

Q. Do you know of any brewer who did not subtract out of gross sales, either under the general legend "cost of goods sold," or some more specific legend, the excise tax?

A. Yes, indeed. I think it is a great distinction between drawing them down before you arrive at net sales and putting them into cost of goods sold—all the difference in the world.

Q. Perhaps we can clarify this. As I understand it, of the nine brewers whose reports you have looked at from the SEC files, and not from the tax return, you found that they included within cost of goods sold, the federal and state excise taxes on beer?

A. No. They did that in the case of one, and that is the ninth example. In the case of the seven to which I referred, they did not include the beer and excise taxes as an item under cost of goods sold. It was treated as a separate deduction from gross sales to arrive at net sales, and there is a great distinction.

Q. But you found no brewer who treated the excise taxes as a deduction of taxes below the line, if I am using the correct accounting phrase?

A. Below the line is not an accounting concept. [59]

Q. On the tax return?

A. I have not seen the tax returns of these nine brewers.

(Testimony of Walter M. Baird.)

Q. In no case did you find a complete elimination of excise taxes as you did find in the case of some state sales taxes?

A. That is true. The items were disclosed in these nine.

Q. You testified as to some practice within the petroleum industry, as to the exclusion of excise taxes. I believe that was your language, that they excluded excise taxes? A. Yes.

Q. How did they exclude their excise taxes?

A. The item of excise tax is not shown either in sales or as a separate deduction from sales, or as a part of cost of goods sold, or as a part of expenses.

Q. What is the nature of those excise taxes that you were speaking of?

A. Federal and state gasoline taxes, primarily; lubricating oil tax.

Q. The federal gasoline tax is a tax on the consumer?

A. I wouldn't feel qualified to say.

Q. You don't know of the nature of the federal and state excise tax on beer, then? [60]

A. Well, I am not a lawyer, I am an accountant. I don't want to start indicating that I understand the legal technicalities of whom the tax is upon. From a good accounting standpoint, it is not too material.

Q. As an accountant, would you say that the term "gross sales" encompasses a broader area than "net sales"? A. Yes.

Q. As an accountant, would you say that the

(Testimony of Walter M. Baird.)

term "gross receipts" encompasses a broader area than "gross sales"?

A. The term "gross receipts" is one that is not clearly defined in accounting. It doesn't have much meaning. Gross receipts to me could entail anything that you put into the bank account, including the borrowing from a bank as a cash receipt, so I don't think you will find, in accounting, the precise definition of "gross receipts." I think accountants look more to sales and to net sales, the way the accounts are usually kept.

Q. So none of your testimony which you have given us here today relates to the question of whether accounting-wise or otherwise, federal and state beer excise taxes should or should not be included in gross receipts?

A. I testified as to what is included normally in gross sales and in net sales.

Q. But not as to gross receipts? [61]

A. I wasn't testifying as to what the law says as to what gross receipts shall include.

Mr. Resnik: I have no further questions at this time.

Mr. Brookes: No further questions of Mr. Baird.

Mr. Resnik: Respondent has no witnesses to offer.

The Court: I don't know that the Petitioner rested.

Mr. Brookes: Your Honor, Mr. Resnik anticipated what I am about to do.

The Court: Before we let this witness leave,

(Testimony of Walter M. Baird.)

there is some reference in one of Mr. Resnik's questions to a name that appeared on a paper that was given him by this witness. That paper isn't in evidence, and I don't say it should be, but I am a little concerned about the way the record will look with that thing hanging in mid-air.

Q. (By Mr. Brookes): Mr. Baird, is that the sheet to which you were referring in your testimony? A. Yes.

Q. Is that the paper from which the figures and the classifications about the practices of different brewers was taken in your testimony?

A. Yes. May I add that in order that no one be deceived as to these nine, these were drawn at random from [62] the breweries, which filed with the SEC. There was no attempt to get certain types. They were drawn at random.

Mr. Brookes: I offer this in evidence, your Honor. That will be Petitioner's Exhibit No. 7.

Mr. Resnik: No objection.

The Court: Received and marked in evidence.

The Clerk: Petitioner's Exhibit 7 admitted in evidence.

(The document referred to was marked and received in evidence as Petitioner's Exhibit No. 7.)

(Witness excused.) [63]

[Title of Tax Court and Cause.]

### CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 24, inclusive, constitute and are all of the original papers and proceedings on file in my office as called for by the "Designation of Contents of Record," including exhibits I thru V, attached to the Stipulation of Facts and Petitioner's Exhibits 6 and 7, admitted in evidence, in the proceeding before the Tax Court of the United States docketed at the above number and in which the petitioner in the Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United States, at Washington, in the District of Columbia, this 9th day of October, 1956.

[Seal]      /s/ HOWARD P. LOCKE,  
Clerk, Tax Court of the  
United States.



[Endorsed]: No. 15334. United States Court of Appeals for the Ninth Circuit. Lucky Lager Brewing Company, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed: October 19, 1956.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for  
the Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

No. 15334

LUCKY LAGER BREWING COMPANY,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

PETITIONER'S STATEMENT OF POINTS  
AND DESIGNATION OF RECORD TO BE  
PRINTED

The point on which petitioner intends to rely is as follows:

Amounts collected by petitioner from its customers to reimburse it for federal and state excise taxes on beer are not part of its "gross receipts" for the purposes of Section 435(e) of the 1939 Internal Revenue Code, and consequently the Tax Court erred in denying petitioner the right to compute its excess profits tax credit on the alternative basis allowed to growth corporations.

Petitioner designates the following portions of the record for printing:

1. The petition to the Tax Court.
2. The answer.
3. The stipulation of facts, excluding all exhibits thereto except the following portion of Exhibit I, which shall be printed: the caption and lines numbered 1 through 15, inclusive, on page 1 of the

United States Corporation Income Tax Return for each of the years 1949 and 1950.

4. The oral testimony of witnesses Jordan and Baird at the trial held on October 4, 1955, as appearing on pages 19 to 63, inclusive.

5. Exhibit 7.

6. The findings of fact and opinion of the Tax Court, filed July 19, 1956.

7. The decision of the Tax Court entered July 23, 1956.

8. The petition for review.

9. The notice of filing petition for review, with acknowledgment of service.

10. Designation of the record on review filed with the Tax Court on October 3, 1956, together with acknowledgment of service thereof.

11. This statement of points and designation of record to be printed.

12. Any counter-designation by respondent.

13. Any stipulation of the parties which may be hereafter filed concerning unprinted exhibits constituting part of record on review.

Dated at San Francisco, California, October 25, 1956.

Respectfully submitted,

/s/ VALENTINE BROOKES,

/s/ ARTHUR H. KENT,

/s/ RUSSEL SHEARER,

Attorneys for Petitioner.

[Endorsed]: Filed October 26, 1956.

[Title of Court of Appeals and Cause.]

STIPULATION CONCERNING EXHIBITS  
NOT PRINTED

The parties hereto, through their counsel, stipulate as follows:

All exhibits contained in the record transmitted to this Court by the Tax Court may be referred to and relied on by either party as constituting part of the record on appeal, whether or not printed in whole or in part.

Dated: November 1, 1956.

/s/ VALENTINE BROOKES,

/s/ ARTHUR H. KENT,

/s/ RUSSEL SHEARER, V.B.  
Attorneys for Petitioner.

/s/ CHARLES K. RICE, J.  
Assistant Attorney General,  
Attorney for Respondent.

[Endorsed]: Filed November 7, 1956.